

ALERTS

California Passes Portions of the Model Money Transmission Modernization Act

October 12, 2023

On Oct. 8, 2023,^[1] California Governor Gavin Newsom signed AB-1116^[2] into law, which amends certain provisions of California's Money Transmission Act (Cal. Fin. Code §§ 2000, *et seq.*) ("MTA") to align with the Model Money Transmission Modernization Act ("Model Law").^[3] The amended MTA will become effective on Jan. 1, 2024. We note the following changes to the MTA that may be of most relevance to California money transmitter licensees:

- Repeals Section 2040(e), which will eliminate the limitation that the aggregate value of a licensee's accounts receivable (excluding money transmission receivables), loans or extensions of credit to any one person (including such person's affiliates) cannot exceed 50 percent of the licensee's tangible net worth without the advanced written approval of the California Department of Financial Protection and Innovation ("DFPI").^[4]
- Adopts the Model Law tangible net worth sliding scale, which will require a licensee to maintain a tangible net worth of "the greater of one hundred thousand dollars (\$100,000) or 3 percent of total assets for the first one hundred million dollars (\$100,000,000), 2 percent of additional assets for one hundred million dollars (\$100,000,000) to one billion dollars (\$1,000,000,000), and one-half of 1 percent of additional assets for over one billion dollars (\$1,000,000,000)."
- Adds additional exemptions from the money transmitter licensing requirements for certain entities, including persons that act as an intermediary by processing money transmission transactions for other

licensed money transmitters or exempt entities subject to certain conditions, and registered futures commission merchants under the federal commodities laws to the extent of their operation as such merchant. The Amended MTA does not amend or repeal any current exemptions from the money transmitter licensing requirements, including the exemption for payroll processors, even though the Model Law expressly includes payroll processing services in its definition of “money transmission.”

- Expressly includes as “eligible securities” funds held in an account held for the benefit of a money transmitter licensee’s customers that is titled “(name of licensee) FBO Its (licensee’s customers or specific group of licensee’s customers).” Currently, to count funds held in FBO accounts as eligible securities, licensees must receive express approval from the DFPI.^[5] We understand that the amendments will eliminate the need to seek DFPI approval for FBO accounts going forward.
- Substantially adopts the list of types of permissible investments (known as “eligible securities” in California) contained in the Model Law, including adding an irrevocable letter of credit that meets certain criteria as a type of “eligible security,” in addition to the FBO account described above.
- Adopts the Model Law definition of “key individual” as a “natural person ultimately responsible for establishing or directing policies and procedures of the licensee, including an executive officer, manager, director, or trustee” and requires a licensee to provide notice to the DFPI within 15 days after the effective date of the key individual’s appointment.
- Adopts a transitional period, which provides that licensees have until Jan. 1, 2025, to comply with any conflicting or new requirements even though the law becomes effective Jan. 1, 2024. We understand that this provision may apply for example, where a licensee is subject to the current \$500,000 statutory tangible net worth requirement. Pursuant to this provision, the licensee would have until Jan. 1, 2025, to increase its tangible net worth requirement to comply with the Model Law’s sliding scale.

While certain provisions in the amended MTA will likely provide welcome relief to licensed California money transmitters, we note that many California licensees have conditions imposed on them via a “Conditions of

Approval” letter issued in connection with the granting of a license, approval of a change of control, or otherwise that may conflict with the amended MTA.[6] It is unclear how the amended MTA will affect these license conditions. The text of the bill, and the accompanying legislative history, do not discuss the interplay between existing license conditions and the amended MTA. We note that the DFPI’s ability to impose conditions on licensees under Section 2036[7] is not affected by the amended MTA. In the absence of guidance from the DFPI, we would recommend that licensees reach out to the DFPI to clarify whether any conditions imposed on them that conflict with the amended MTA are now superseded by such amendments or if the licensee needs to formally seek relief from the DFPI.

Schulte Roth & Zabel’s lawyers are available to assist you in addressing any questions you may have regarding these developments. Please contact the Schulte Roth & Zabel lawyer with whom you usually work, or any of the following attorneys:

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[1] Office of Governor Newsom, *Governor Newsom Issues Legislative Update 10.8.23* (Oct. 8, 2023), available at <https://www.gov.ca.gov/2023/10/08/governor-newsom-issues-legislative-update-10-8-23/>.

[2] AB-1116 Money Transmission Act (2023-2024), *available at* https://leginfo.legislature.ca.gov/faces/billNavClient.xhtml?bill_id=202320240AB1116.

[3] CSBS Model Money Transmission Modernization Act, *available at* <https://www.csbs.org/sites/default/files/2023-08/CSBS%20Money%20Transmission%20Modernization%20Act.pdf>.
The following states have also adopted portions or the substantial entirety of the Model Law: Arizona, Arkansas, Connecticut, Georgia, Hawaii, Indiana, Iowa, Minnesota, Nevada, New Hampshire, North Dakota, Rhode Island, South Dakota, Tennessee, Texas, Utah, and West Virginia. CSBS, *2023 Money Transmission Modernization Act Legislation* (Aug. 30, 2023), *available at* <https://www.csbs.org/sites/default/files/2023-08/2022%20and%202023%20MTMA%20update%208-30-2023.pdf>

[4] The current language of Section 2040(e) reads as follows: “The aggregate value of a licensee’s accounts receivable, excluding money transmission receivables, loans or extensions of credit to any one person, or that person’s affiliates, cannot exceed 50 percent of the licensee’s tangible shareholders’ equity without the advanced written approval of the commissioner.” Cal. Fin. Code § 2040(e).

[5] *See* Cal. Fin. Code § 2084.

[6] For example, licensees may be subject to a condition to maintain a tangible net worth that is higher than the Model Law sliding scale.

[7] “The commissioner may impose on any authorization, approval, license, or order issued pursuant to this division any conditions that are necessary for the safety and soundness of the licensee, or reasonable or necessary to maintain or enhance consumer protection.” Cal. Fin. Code § 2036.

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