



# The Legal 500 Country Comparative Guides

## United States: Fintech

This country-specific Q&A provides an overview of fintech laws and regulations applicable in United States.

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## **1. What are the sources of payments law in your jurisdiction?**

Payments laws in the United States consist of an array of regulatory regimes administered by both state and federal regulators. The primary purpose of these regimes is to protect consumers, facilitate orderly and efficient transfers of value and prevent money laundering and other illegal activities involving payments.

At the federal level, payments touch a number of financial industry statutes and regulations, including the Consumer Credit Protection Act, Bank Secrecy Act, Gramm-Leach-Bliley Act, Electronic Funds Transfer Act and Reg. E, Dodd-Frank Act, Expedited Funds Availability Act, Reg. CC, Reg. J, Reg. II, and the Uniform Commercial Code. At the state level, payments are generally covered by money transmission, auto-renewal, surcharge, and prepaid access laws. The federal and state statutory regimes governing payments is supported by periodic rulemakings and guidance issued by regulators.

In addition to governmental oversight, the payments industry has developed certain standards by which participants must abide. For example, the Payment Card Industry Security Standards Council administers and maintains payment card industry data security standards (PCI-DSS) for those who process, store or transmit cardholder data. Similarly, the National Automated Clearing House Association (NACHA) issues operating rules and guidelines for automated clearing houses (ACH) while the major card networks – American Express, Discover, MasterCard – each have sets of rules governing card payments facilitated on their respective payment rails.

## **2. Can payment services be provided by non-banks, and if so on what conditions?**

Yes. With the growth of fintech, and embedded finance specifically, it is becoming increasingly more common for non-banks to offer payment services. Generally, at the federal level, an entity that facilitates the transfer of funds or equivalent forms of value must register as a Money Services Business (MSB) with the Financial Crimes Enforcement Network (FinCEN). Those registrations generally require the implementation of policies and procedures to comply with the Bank Secrecy Act, as well as recordkeeping, reporting, transaction monitoring, and other regulatory requirements. Additionally, for those registered as a MSB, there will be state-level money transmitter obligations largely aimed at ensuring consumer protection.

With the growth of fintech/bank partnerships and the Banking-as-a-Service model (BaaS), it has become increasingly more common for non-bank financial services providers (including payments) to enter into sponsorship or program management arrangements with banks. These relationships subject payment service providers to supervision by the prudential regulators that supervise their bank partners.

## **3. What are the most popular payment methods and payment instruments in your**

## **jurisdiction?**

Even prior to COVID-19 the utilization of cashless and app-based forms of payment were on the rise. However, COVID-19 has amplified the growth of cashless, peer-to-peer, in-app, and online payments. In addition, while cryptocurrency payments have not yet been widely adopted, the number of businesses starting to accept cryptocurrencies as payment for products and services, or are at least integrating a framework to do so, is increasing.

Furthermore, the use of point-of-sale financing (POSF) as an alternative to cash or traditional credit continues to increase in the United States as more POSF platforms are embedded into the “checkout” process of online retailers. POSF providers offer the ability for a consumer to be efficiently underwritten and offered a credit product (most commonly a term loan) to finance their purchase.

#### **4. What is the status of open banking in your jurisdiction (i.e. access to banks’ transaction data and push-payment functionality by third party service providers)? Is it mandated by law, if so to which entities, and what is state of implementation in practice?**

Open banking is not mandated by law in the United States, although the concepts of open banking are becoming commonplace as a result of consumer and commercial preferences for quicker and more efficient digital-first financial services. For example, digital infrastructure service providers are regularly integrating with financial institutions through APIs in order to facilitate a variety of services, including account aggregation and data utilization. While prudential regulators such as the FDIC have issued guidance about open banking and banks’ use of third party service providers, specific open banking regulations have not been promulgated. Therefore, open banking services remain subject to contractual requirements agreed to by third party service providers and banks, terms of use with customers, and bank regulator oversight.

#### **5. How does the regulation of data in your jurisdiction impact on the provision of financial services to consumers and businesses?**

Data privacy regulation is a significant consideration for fintech and traditional financial institutions, and plays a meaningful role in the operational, compliance and analytics functions of those entities as well as their service providers. The use of data is governed at the federal level under the Gramm-Leach-Bliley Act (GLBA), Fair Credit Reporting Act (FCRA), Right to Financial Privacy Act (RFPA), Bank Secrecy Act (BSA), and USA PATRIOT Act. In addition, some states have robust data privacy regulations. For example, the California Consumer Privacy Act (CCPA) imposes numerous restrictions on the handling and processing of California residents’ data. Additionally, all fifty states have some form of data breach notification laws.

Additionally, banks and their service providers have compliance obligations relating to data

security as well as consumer protection regulation requiring consents and disclosures to users of services. To comply with these obligations, financial institutions and fintech platforms must implement robust security programs designed to protect customer data and ensure its use in accordance with the terms under which such data was acquired.

**6. What are regulators in your jurisdiction doing to encourage innovation in the financial sector? Are there any initiatives such as sandboxes, or special regulatory conditions for fintechs?**

Both federal and state regulators have launched initiatives to facilitate compliant innovation. At the federal level, the Commodity Futures Trading Commission (CFTC) launched LabCFTC in 2017 to promote and facilitate innovation in the commodities and derivatives industry through closely studying developments in technology, issuing explanatory primers, and speaking with industry participants. LabCFTC liaises between innovators and the other CFTC divisions. In October 2019, the Chairman of the CFTC announced that LabCFTC was elevated to an independent operating office of the CFTC that reports directly to the Chairman. The Securities Exchange Commission (SEC) launched its Strategic Hub for Innovation and Financial Technology (FinHub) in 2018 to educate innovators in the securities industry and facilitate regulatory compliant innovation. Similar to LabCFTC, FinHub sometimes serve as liaison between innovators and the SEC staff.

Additionally, the Office of the Comptroller of the Currency (OCC) and the Consumer Financial Protection Bureau (CFPB) each created Offices of Innovation to support responsible innovation and to foster open communication amongst banks, fintech platforms and the regulatory bodies that oversee them. The CFPB is one of several financial regulators around the world participating in the Global Financial Innovation Network (GFIN), an initiative launched in 2019 to create a “global sandbox”. The aim of GFIN is to facilitate efficient communication with various regulators, and allow the regulators to collaborate and share their experiences fostering innovation with one another. The CFPB has also launched a Trial Disclosure Sandbox that allows companies to develop and test innovative means of improving the content and delivery of consumer disclosures.

At the state level, several states including Wyoming, Arizona, and Utah have established regulatory sandboxes. These sandboxes provide a means for innovators and regulators to collaborate on new products or services in an environment intended to foster innovation.

**7. Do you foresee any imminent risks to the growth of the fintech market in your jurisdiction?**

While consumer and commercial sentiments are expected to drive continued growth of the fintech market and use of fintech products and services, the growth in the United States is not without risks to be navigated. Perhaps the biggest risk to fintech in the United States is regulatory uncertainty. For example, there is no federal legislation providing framework for the regulation of cryptocurrency. As a result, regulation has developed in a piecemeal fashion

amongst multiple federal agencies (primarily the SEC, CFTC, and FinCEN) through guidance, informal rulemaking, and even public statements by staff and commissioners. This is just one example of where clarity of regulatory boundaries makes it challenging for innovators and fintech companies to create new products and services with the required regulatory certainty needed for mass adoption.

## **8. What tax incentives exist in your jurisdiction to encourage fintech investment?**

The United States does not provide any U.S. federal income tax (USFIT) incentives that are specific to the fintech industry. However, changes to USFIT law that generally took effect in 2018 have made the United States a more attractive jurisdiction in which to pursue technology-based businesses, including fintech. For example, 2018 saw a significant reduction in the corporate USFIT rate, from 35% to 21%. Furthermore, an incentive rate of 13.125% may apply to intangible-based business income of a U.S. corporation that is earned from sources outside of the United States. This incentive rate, coupled with a new penalty tax meant to discourage investment in the technology sector outside of the United States, was introduced with the intent of increasing technology investments in the United States, although the ultimate impact of these new rules is subject to ongoing debate (the incentive rate is scheduled to become less generous beginning after December 31, 2025, although the penalty tax will also become more severe at the same time).

Additionally, USFIT laws generally contains various incentives. For example, the Research and Development Tax Credit (R&D Credit) encourages innovation and technology investment and may be available to fintech companies. Fintech investors may also be able to take advantage of USFIT incentives designed generally for emerging or expanding companies such as investing in fintech companies whose stock qualifies as Qualifies Small Business Stock.

## **9. Which areas of fintech are attracting investment in your jurisdiction, and at what level (Series A, Series B etc)?**

Although it appears that United States fintech investment activity in 2020 will fall short of the record year seen in 2019, the level of investment (as measured by dollar volume and transaction count) remains strong despite the effects of the COVID-19 pandemic. While time will tell, many believe that COVID-19 will accelerate fintech growth and related investments due to the increased need for digital infrastructure and technology based redundancies to account for growth of online businesses, digital payments and cloud-based financial services.

Specific areas where investment and growth remain strong are digital banking infrastructure, contactless and in app payments, artificial intelligence and machine learning, distributed ledger technology and data analytics. Furthermore, the increased adoption of the banking-as-a-service (BaaS) model and the scale of digital-first challenger banks continues to provide investment opportunities ranging from seed to growth stage.

**10. If a fintech entrepreneur was looking for a jurisdiction in which to begin operations, why would it choose yours?**

Despite the regulatory complexity, which some operators view as a positive and welcomed differentiator, the United States is a highly compelling jurisdiction for any fintech entrepreneur or company to launch or scale their business.

First, the total addressable market is significant and ripe for innovation regardless of whether you are offering a business-to-business solution or a direct-to-consumer product or service. For example, traditional financial institutions such as banks, insurance companies and credit unions largely operate on legacy technology and actively seek to implement systems and relationships to better position themselves for the flexibility required to operate as digitally minded organizations. Similarly, consumers and businesses alike exhibit clear preference for intuitive online and mobile application based fintech offerings that operate with the ease of use and functionality they have come to expect from their financial services.

Second, access to advisory resources such as incubators and capital providers ranging from venture capital and private equity, to angel and seed investor networks, remains strong.

Whether measured by dollar or transaction volume, North America (largely driven by investments in the United States) continues to outpace Europe, Asia and other jurisdictions for both private and public financing.

**11. Access to talent is often cited as a key issue for fintechs - are there any immigration rules in your jurisdiction which would help or hinder that access, whether in force now or imminently? For instance, are quotas systems/immigration caps in place in your jurisdiction and how are they determined?**

There are several visa categories that fintechs may use to access talent, yet each of these areas contains certain restrictions. Additionally, while the U.S. Citizenship and Immigration Services (USCIS) is currently processing petitions, due to the COVID-19 pandemic there may be significant delays.

The H-1B program allows fintechs to employ foreign workers in certain specialty occupations in areas such as science, engineering and information technology. Petitions are subject to congressionally-mandated caps each year. For FY 2021 H-1B cap-subject petitions, petitioners should expect longer than usual delays as USCIS has delayed data entry and receipt notice generation due to the impacts of COVID-19.

Students on an F-1 visa may obtain temporary employment through Optional Practical Training (OPT) in areas directly related to their field of study. After a student completes her studies, she may apply to work in post-completion OPT for a limited time period. Additionally, if a student has earned degree in certain science, technology, engineering, and math fields,

she may apply for a 24-month extension of her OPT employment authorization subject to certain requirements (including the employer's participation in E-Verify).

In addition to these restrictions, on June 22, 2020 the President of the United States issued a *Proclamation Suspending Entry of Aliens Who Present a Risk to the U.S. Labor Market Following the Coronavirus Outbreak*, which suspended and limited entry into the United States by individuals seeking entry pursuant to certain nonimmigrant visas, including, among others, an H-1B visa, subject to certain exceptions. Currently, this restriction is set to expire on December 31, 2020.

**12. If there are gaps in access to talent, are regulators looking to fill these and if so how? How much impact does the fintech industry have on influencing immigration policy in your jurisdiction?**

Fintechs and related industry groups continue to oppose congressionally-mandated limits on visas for skilled foreign workers. While Congress has considered a number of legislative efforts to raise or eliminate such limits and caps, to date such efforts have been unsuccessful. Fintechs and related industry groups have also challenged various actions by USCIS and related federal agencies in court. Most recently, a coalition of technology companies and industry groups have challenged the President's June 22 action suspending entry of certain individuals into the United States in a lawsuit currently in the Northern District of California (*National Assoc. of Manufacturers et al. v. Dep't of Homeland Security et al.*, Case No. 3:20-cv-04887 (N.D. Cal. filed Jul. 21, 2020)).

**13. What protections can a fintech use in your jurisdiction to protect its intellectual property?**

In the United States Fintech companies can benefit from a comprehensive, multi-faceted approach and structured plan to protect intellectual property (IP) associated with their technology.

As the majority of the operational portion of the IP will be in the form of software, it is important to spend time as early as possible (and during development of improvements) to set the development parameters to ensure ownership and control over the code and to take steps to protect the related IP. This includes protections for such software portions as the front-end code, backend code, APIs, and database structures. A useful method of IP protection for critical algorithms embedded in the code is trade secret. Trade secret protection means protecting such information and translates into locking down and protecting the source code. Additionally, policies related to use of open source code integrated into or linked to the proprietary portions of code are critical to ensure against viral "copyleft" licenses from being integrated that require disclosure of source code.

When proprietary code is created, common law copyright rights immediately vest in the fintech company that created it. In some cases, companies file registered copyrights on all or

portions of the code and most often in object code form.

Patent protection is also often pursued by fintech companies. Review of potential inventions to determine those most likely to lead to patent protection and decisions to file to attempt to achieve such patent protection instead of resorting to trade secret protection must be evaluated. Once the decision to file is made, software patents must be carefully drafted and prosecuted to maximize the potential of issuance and result in claims of useful scope.

Finally, an important form of IP protection is registration of trademarks to protect the brand name as well as its logos, slogans, and other indications or origin of a fintech company's products. Such trademarks differentiate a fintech company's products from those of competitors and allow the company's products to generate value in the form of goodwill that contributes to its bottom line valuation.

**14. How are cryptocurrencies treated under the regulatory framework in your jurisdiction?**

There is no central regulatory or statutory framework that governs cryptocurrencies in the United States. As a result, multiple federal and state regulatory regimes may be applicable based on the attributes of the cryptocurrency and its corresponding blockchain ecosystem, including the facts around how it was developed.

Depending on the circumstances, cryptocurrencies may be subject to federal or state regulations governing securities, derivatives, commodities, money transmission, data privacy, tax and any industry-specific regulations. With respect to newly developed cryptocurrencies perhaps the most important question is whether—based on the facts around its development, issuance, and characteristics—the cryptocurrency is a security or commodity. The answer will determine whether the cryptocurrency and the developing entity are subject to significant regulatory oversight by the SEC or the CFTC's enforcement authority over commodities (assuming that the cryptocurrency does not underlie a derivatives instrument, in which case such instrument will be subject to CFTC regulatory oversight). Additionally, cryptocurrency exchanges that facilitate the buying and selling of cryptocurrencies will be subject to money transmission regulation overseen at the federal level by FinCEN and the state level by the appropriate state regulator.

**15. How are initial coin offerings treated in your jurisdiction? Do you foresee any change in this over the next 12-24 months?**

The SEC, the federal agency responsible for enforcing securities laws and regulating securities markets in the United States, is the primary regulator with an interest in Initial Coin Offerings (ICOs). The SEC aims to ensure that ICOs are conducted properly and that investors in ICOs are treated fairly. Over the past few years, the SEC has used its enforcement authority to initiate investigations and bring actions against ICO issuers asserting that ICOs are "investment contracts" (as defined in the seminal case used to

determine when a cryptocurrency is actually a security *SEC v. W.J. Howey Co.*), and therefore illegal unregistered securities offerings.

In 2019, the SEC published a framework for entities developing blockchain projects that include a corresponding cryptocurrency to consider. The framework lays out in detail the factors (based largely on the factors of the *Howey* test) that the SEC weighs when determining if a cryptocurrency is a security. That framework was accompanied by a “no action letter” to TurnKey Jets, whose project sought to leverage a crypto based token. Applying its framework, the SEC did not consider the token a violation of securities laws.

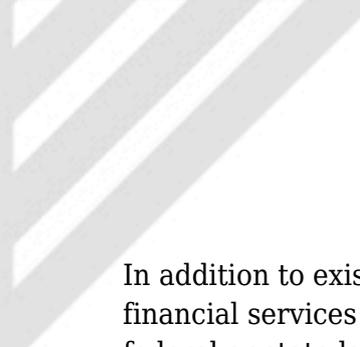
Since the TurnKey Jets no action letter, the SEC has continued to pursue companies and platforms seeking to leverage cryptocurrencies or tokenization projects in violation of the registration provisions of federal securities laws. In particular, the SEC secured an injunction in federal court against a prominent blockchain project—preventing the project from launching—on grounds that the issuance of the blockchain’s corresponding cryptocurrency would be an unregistered securities offering. The SEC has also brought and settled matters with several other blockchain-based services companies charged with conducting unlawful securities offerings. Over the next 12-24 months we expect to continue to see companies that previously issued illegal unregistered digital securities take actions to rectify their violations, as well as the SEC to continue to pursue those who do not.

**16. Are you aware of any live blockchain projects (beyond proof of concept) in your jurisdiction and if so in what areas?**

The U.S. is home to hundreds of operational blockchain projects and companies whose technology and infrastructure utilize blockchain technology. These companies and projects span every major industry including financial services and banking, healthcare, pharmaceuticals, insurance, agriculture, real estate, gaming, cybersecurity and data protection. Given that leveraging blockchain technology provides industry agnostic benefits, there is no reason that its use, adoption and scale should not continue in the United States.

**17. To what extent are you aware of artificial intelligence already being used in the financial sector in your jurisdiction, and do you think regulation will impede or encourage its further use?**

The rise of AI and machine learning technology coupled with increased customer expectations for quick and efficient financial services has led to significant acceleration in the use of AI and machine learning for the financial sector in the United States. AI is leveraged to help financial service providers process, analyze and use data faster and more accurately. The utilization of AI has become common in underwriting, risk management, investment advice, financial product trading, data analysis and pattern recognition, conversational customer service, fraud detection and cybersecurity. The acceleration of the use of AI has been on a first-party basis where a financial service provider leverages its own AI tools, as well as on a third-party basis provided by third-party service providers or vendors.



In addition to existing state and federal laws that regulate the conduct and operations of financial services firms and their third-party service providers, there are few AI-specific federal or state laws. However, there are a number of pieces of federal legislation that have been introduced in 2020 focused on regulating AI or increasing funding for the research, development and education of AI. Such legislation includes the National Cloud Computing Task Force Act, the Advancing AI Research Act of 2020, and the National Artificial Intelligence Initiative Act. As the use of AI by various financial sector participants increases, we expect that new and additional legislation will play a meaningful role in shaping the growth of this market.

**18. Insurtech is generally thought to be developing but some way behind other areas of fintech such as payments. Is there much insurtech business in your jurisdiction and if so what form does it generally take?**

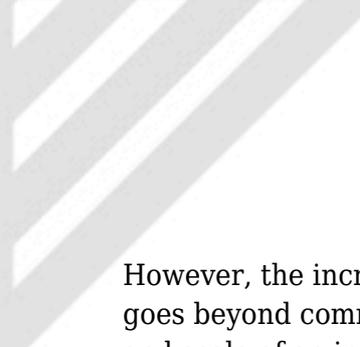
The U.S. InsurTech market is comprised of two main verticals. The first includes technology companies developing innovative products or services utilized by insurance providers who offer life, property and casualty or health insurance products. The second includes companies who leverage technology and innovative digital-first business models to deliver insurance products or services direct to the insureds, in a manner intended to disrupt or supplement the traditional insurance supply chain. Although 2020 will likely see a less active market for InsurTech (as measured by financing and M&A volume) than the banner year seen in 2019, the utilization of InsurTech by insurance companies and consumers continues to grow.

**19. Are there any areas of fintech that are particularly strong in your jurisdiction?**

The United States has proven to be a strong jurisdiction for fintech innovation and adoption, and a valuable one for continued investment as a result of the ongoing efforts of traditional financial institutions to become more digitally focused. Among the United States' areas of prominence are banking infrastructure to support functions such as data aggregation and utilization, payments, and online or app based investing.

**20. What is the status of collaboration vs disruption in your jurisdiction as between fintechs and incumbent financial institutions?**

Although fintech companies who seek to disrupt traditional financial institutions remain, the balance has largely shifted away from the messaging and ambitions to disrupt the incumbents in favor of a more collaborative fintech ecosystem. For example, fintech companies in large part realize the value in working with banks, and not against them, given certain aspects unique to banks such as their lower cost of funds due to the deposits they hold. Additionally, while the level of adoption and integration between banks and fintech companies has never been higher, the rise of the banking-as-a-service (BaaS) model where state and federal chartered banks act as a sponsor or program manager for a fintech company is only increasing bank/fintech collaboration.



However, the increase in collaboration amongst financial institutions and fintech companies goes beyond commercial relationships. Another area of focus in 2020 has been the launch and scale of an increased amount of corporate venture capital divisions focused on investing in fintech businesses, as well as internal incubators and innovation labs by many prominent financial institutions.

**21. To what extent are the banks and other incumbent financial institutions in your jurisdiction carrying out their own fintech development / innovation programmes?**

Incumbent financial institutions have increased development of fintech through in-house initiatives, as well as formal collaborations and partnerships with fintech companies. Financial institutions recognize that legacy technology is restraining their ability to manage the in-flow of large amounts of data, comply with regulatory obligations and respond to customer demands. As a result, incumbent institutions are using various channels to develop and implement fintech solutions.

**22. Are there any strong examples of disruption through fintech in your jurisdiction?**

The increased use of mobile wallets and app-based payment services is one of the larger disruptions or market shifts in the United States as consumers continue to move away from physical cards in favour of smartphones for online and proximity payments. These fintech tools provide fast, secure and often a cheaper means to spend, transfer and save money.

While millennials were the early adopters of these fintech services for functions such as peer-to-peer payments and splitting bills, the utilization of these services for consumers and businesses alike has scaled across a broader demographic in 2020.