



Financial Services Management

Nonbank Payment Provider CFPB Supervision

Cite

CFPB, Notice of Proposed Rule, Defining Larger Participants of a Market for General-Use Digital Consumer Payment

Recommended Distribution

Payments, Retail Finance, Policy, Legal, Government Relations

Website

https://files.consumerfinance.gov/f/documents/cfpb_nprm-digital-payment-apps-lp-rule_2023-11.pdf

Impact Assessment

- CFPB supervision will reduce nonbank regulatory-arbitrage competition resulting from less stringent compliance, expectations that certain standards are inapplicable, and other disparities between bank/nonbank regulation/enforcement.
- CFPB authority extends only to consumer protection, but the agency is likely to use its supervisory power also to address payment-system resilience, reliability, and privacy concerns.
- The agency's definition of consumer protection also extends to supervision aimed at blocking data monetization and digital marketing. Although this proposal is aimed at nonbanks, this interpretation is likely also to apply to CFPB large-bank, service-provider payment-system supervision.

Overview

Building on its director's longstanding focus on fintech and tech-platform companies, the CFPB has proposed to extend its supervisory reach to nonbank providers of general-use digital payments services. The Bureau's definition of these terms is broad and thus would bring almost all covered nonbank services into its ambit with considerable potential for subsequent demands for significant operational change along with heightened legal and reputational risk. The extent to which the Bureau pursues the ends enabled by this proposal remains to be seen, but it could set high roadblocks restricting the network-effect benefits major tech-platform companies have long enjoyed not only due to real and perceived regulatory exceptions, but also by virtue of their financial and commercial activities.

Impact

The Bureau bases this proposal on provisions in its authorizing statute allowing it to supervise "larger" consumer-finance market participants following rulemaking to this

effect as well as any nonbank it has specific reason to believe poses a consumer-protection threat following notice to any such company and an opportunity for it to protest.¹ This proposal focuses on defining larger participants to set supervisory standards for fintech and tech-platform companies providing general-use digital consumer-payment services, laying the groundwork for doing so following issuance of an entity-specific order should the Bureau then deem this appropriate. The Bureau believes seventeen companies would come under possible Bureau supervision, accounting for 88 percent of transactions in this arena.

The statute and this proposal deal only with supervision; the law otherwise requires nonbanks to comply with CFPB rulemakings and related enforcement. Notably, the Bureau believes that, once it has established its right to supervise an entity, it has the authority to supervise all activities and purposes under its authority, not just those specified by the rule or order expressly authorizing supervision. As a result, the rule has significant bearing not only on the products and services it directly covers (see below), but also on all consumer-finance activities of entities that come under it.

Services expressly covered by this proposal include digital wallets, payment apps, funds-transfer apps, P2P payment apps, and like-kind services. Several of these services are often considered “money services” for purposes of state regulation, with providers either coming under or in some cases seeking state charters to gain the right to operate nationwide or refute the need for federal regulation. The rule acknowledges the scope of state regulation in this area but promises only to coordinate with state agencies.

The Bureau’s definition of general-use digital consumer payments is also broad, including for example a digital wallet in which a consumer has provided a credit card and the wallet executes the transaction. Supervision would also extend to nonbanks providing payment services for goods or services purchased on their marketplace provided by third-party sellers even though they would not be covered if the services are in connection with consumer purchase of their own goods or services. However, as detailed below, using payment data related to own goods-and-services sales might still be considered general-use and thus subject to CFPB supervision if the entity uses these data for purposes such as digital marketing.

This provision is clearly meant to apply to tech-platform companies and thus expands CFPB power likely designed to ensure that these companies avoid conflicts of interest, protect privacy, and otherwise comport themselves in accordance with CFPB concerns when it comes to digital marketing.² This and certain other aspects of the definition of covered transactions are broader than those now covered by relevant rules, creating broad reach for CFPB supervision. This could arguably extend the Bureau’s reach into areas not now clearly regulated for like-kind bank transactions, adversely affecting the Bureau’s level-playing field rationale. However, large banks are already subject to CFPB supervision and, where they are parties to credit transactions related to a payment, they come under both consumer-protection and safety-and-soundness standards. They are also barred from commercial activities.

¹ See **CONSUMER14**, *Financial Services Management*, July 19, 2010.

² See **FINTECH30**, *Financial Services Management*, August 15, 2022.

The Bureau includes a cost-benefit analysis of the proposal that finds its costs hard to anticipate due in part to the uncertain nature of how many companies will be subject to CFPB supervision. Further, companies that improve compliance to deter supervision will incur costs the Bureau does not attribute to the proposal even though it notes benefits resulting from enhanced adherence to governing law and rule. Other anticipated benefits are better consumer protection and fair competition.

What's Next

The CFPB released this proposal on November 7; comment is due by the later of January 8 or thirty days after *Federal Register* publication.

Analysis

Covered nonbanks and their affiliates are those which:

- provide covered digital general-use consumer payments with an annual transaction volume of at least five million payments. The Bureau notes that some entities do hundreds of billions of transactions but it has set the threshold low to capture larger providers in key sectors, seeking comment on this measure; and
- not be a small-business as defined by the SBA.

The Bureau asserts that it has the authority to demand books and records to determine covered large participants and intends to do so with this standard. Entities would receive written notice that they are deemed larger participants and, as noted, have the opportunity then to object.

Entities covered are those providing a covered payment functionality through a digital application for a consumer's general use in making consumer payment transactions. Functionality is defined to include funds transfers and wallets; payment transactions would be defined as a transfer of funds by or on behalf of a consumer to another person for personal, family, or household purposes, with this term also applicable if credit is part of the transaction or funds are transferred in connection with purposes from the nonbank using only the nonbank's payment services. Use of a company's or an affiliate's digital-payment app to facilitate consumer purchase goods or services from an unaffiliated provider on the payment-service provider's marketplace also leads to a covered transaction, as would using consumer data related to payments for monetization, digital marketing, or "research."

Cryptoasset payments are also covered. However, a consumer must be physically located in a U.S. state for the Bureau's supervisory authority to apply. Excluded transactions would be international money transfers, fund/fund transactions (e.g., foreign exchange, crypto) and for purchasing securities or commodities, use of a commercial provider's own services (although the Bureau has authority over these under separate authority), and use of the digital platform to obtain credit from the provider or its affiliate constitutes a covered transaction.

The proposal also defines "general use" to include P2P payments even if these are on closed loops, even those related to prisons, on the grounds that entry is open to participants and funds may be used in unrestricted ways even if the prisoner must way

to be released to do so. However, payment apps used solely to purchase restricted goods or services (e.g., transport, gift cards, a specific financial service) are not general use. Comment is solicited on these definitions as well as on many others (e.g., for “digital and “personal device”) in the proposal.