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Via Electronic Mail

The Honorable Douglas Ducey
Governor of Arizona
1700 West Washington Street
Phoenix, Arizona 85007

Re: Request for a Veto of House Bill 2177

Dear Governor Ducey:

The Center for Economic Integrity strongly urges you to veto House Bill 2177. The Center is a Tucson-based nonprofit organization founded in 2001 with a mission to build economically strong communities for all and oppose unfair corporate and government practices. We support effective consumer protections for financial services and products to safeguard Arizona families.

Last year the Legislature enacted HB 2434 to create a Regulatory Sandbox Program for financial products and services in the Office of Attorney General. The idea was to permit “innovative” financial services to be tested on Arizona consumers without licensing, supervision and enforcement by the Arizona Department of Financial Institutions that would otherwise apply. No evidence was presented to demonstrate that the Administration thwarted innovation in the financial services market. We opposed HB 2434 to create duplicative government oversight of business without protecting consumers. We continue to believe that deregulation is not necessary to foster innovations that benefit the state’s economy nor is it prudent to put Arizona consumers at risk.

This year, Rep. Weninger sponsored HB 2177 to expand the Arizona sandbox before the program has established any track record of protecting consumers while fostering innovation in the financial services market. The sandbox has been open for eight months and only four companies have been admitted to date. To the best of our knowledge, none of the products are on the market and few if any customers are testing the money transmitter, consumer lender, and car title loans to be offered by these participants. The governor’s office and the legislature have not received the first required annual report from the Attorney General on Arizona’s experience with the sandbox. There is no track record for Arizona’s sandbox.

HB 2177 seeks to expand the Regulatory Sandbox Program and to consolidate authority in the hands of the Attorney General. HB 2177:

- **Removes the cap on the number of consumers** who can use the test products during the period between when a participant reaches the limit (up to 17,500 consumers) and when a license is obtained. Before there are any customers, this bill removes the cap.
- **Expands eligibility to companies that are not required to be licensed** by the Arizona Department of Financial Institutions or registered with the Arizona Corporation Commission. Why would a fintech company not required to be licensed want to enter the sandbox? One benefit is a boost for raising investment and capital. Given the Attorney General’s unilateral authority to grant entry and to expel participants, *this expansion permits one elected official to create winners and losers in Arizona’s market.* There is no need to expand the sandbox by admitting companies that do not need to be licensed in the first place.
- **Removes the requirement that testers be citizens of Arizona** for money transmitter transactions. Restricting sandbox testing to state residents was one of the parameters in last year’s bill. Before a money transmitter test is conducted, this limit is removed.
- **Grants that the Attorney General “alone”** shall enforce laws regarding sandbox participants. That means the OAG that has unilateral authority to grant entry to the sandbox also is the only government agency that can bring law enforcement actions. Since at least three participants have mandatory arbitration clauses and bans on class action lawsuits, consumers are shut out of the courts and cannot bring cases under the Consumer Fraud Act as a result. This amendment concentrates all authority to police companies in the sandbox in one person.

Arizona’s Regulatory Sandbox Program Creates More Government but Less Consumer Protection

- Operating a financial services Regulatory Sandbox Program in the Office of Attorney General duplicates the job of the Arizona Department of Financial Institutions and the Arizona Corporation Commission to license, supervise, examine and enforce the law with the categories of business under their purview.
- Providing two choices of regulator for financial services companies creates regulatory arbitrage. Companies can choose to be licensed by the Department of Financial Institutions or registered to operate in the Attorney General’s Sandbox. Will these agencies compete to protect consumers or to ease entry into Arizona’s market for fintech firms?
- At \$500 per sandbox applicant, it is unlikely that revenue will cover the cost of the Sandbox program. What is the Attorney General’s office not able to do because it has expanded its portfolio of duties to economic development and financial services regulation?

HB 2177 fails to close the glaring consumer protection holes in the Sandbox law.

The *Financial Times* reported in December that the Arizona sandbox was promoted in the UK as “Arizona State Offering Regulation-free Access for UK Companies.” (Jemima Kelly, “[A ‘fintech sandbox’ might sound like a harmless idea. It’s not.](#)” *Financial Times*, December 5, 2018)

Money transmitters in the sandbox are not required by the sandbox law to hold surety bonds, comply with permissible investment rules, have adequate liquid assets to conduct business or meet a legal standard to complete transactions. The anti-money laundering reporting requirements of Arizona law do not apply. Money transmitters regulated by your Department of Financial Institutions are subject to basic safety requirements. Money transmitters in the Attorney General’s sandbox should also be subject to Sections 6-1205; 1205.1; 1212; 1214; 1241 and 1242.

While the Attorney General can require individual companies to comply with any provision of state law, there is no reason to believe that money transmitters in the sandbox are being made subject to statutory protections. We believe that consumers and the market should be protected by requiring all money transmitters in the sandbox to adhere to basic safety and soundness requirements. This is especially important because low-income consumers rely on money transmitters to handle their funds and because cryptocurrency exchanges are considered money transmitters.

Despite the urging of several public interest witnesses, the backers of Arizona’s sandbox refused to amend the bill to protect users of money transmitters.

HB 2177 fails to require all lenders to play by the same set of rules. Consumer Lenders in the sandbox that can make installment loans up to \$15,000 secured by borrowers’ vehicles are subject to Arizona’s usury law that caps rates at 36 percent annual interest plus a 5% fee and are required to comply with strong consumer protections. Title Lenders in the sandbox that can make unlimited size loans secured by borrowers’ vehicles can make asset-based loans that cost up to 204% APR and have balloon payment terms.

Despite the urging of several public interest witnesses, the backers of Arizona’s sandbox refused to amend the bill to require all lenders to comply with Arizona’s 36% usury law.

The Center for Economic Integrity requests that you veto House Bill 2177. We urge you to require that Arizona’s Regulatory Sandbox Program protect consumers by requiring the statutory protections of the Money Transmitter law apply to sandbox money transmitter participants and by requiring that Arizona’s usury law apply to all secured and unsecured consumer loans made by sandbox participants. Please let us know if you have any questions or if I can provide you with any additional information,

Sincerely,



Kelly Griffith
Executive Director