STATE OF NEW YORK

9899--A

IN ASSEMBLY

February 21, 2018

Introduced by M. of A. KIM, VANEL, QUART, SEPULVEDA, D'URSO, RA -- Multi-Sponsored by -- M. of A. LUPARDO -- read once and referred to the Committee on Banks -- committee discharged, bill amended, ordered reprinted as amended and recommitted to said committee

AN ACT to amend the financial services law, in relation to creating a regulatory sandbox program; to amend the banking law, in relation to safeguarding financial technology products and services and prohibiting licensing fees for such products and services; and providing for the repeal of such provisions upon expiration thereof

The People of the State of New York, represented in Senate and Assembly, do enact as follows:

Section 1. The financial services law is amended by adding a new article 7 to read as follows:

ARTICLE 7

REGULATORY SANDBOX PROGRAM

Section 701. Definitions.
702. Reports; studies.
703. Program purpose.
704. Application process and requirements.
705. Consultation with applicable agencies; admission authority; scope; insurance products; investment management.
706. Consumer protection.
707. Exit requirements.
708. Extensions.
709. Auditing by third party depository or custodian services.
710. Recordkeeping and reporting requirements.
711. Records; disclosure; evidentiary effect.
712. Reporting requirements; monitoring; enforcement; agreements.

§ 701. Definitions. For purposes of this article, the following terms shall have the following meanings:

(a) "Securities investor protection corporation" means a federally mandated, non-profit, member-funded, United States corporation created

EXPLANATION--Matter in *italics* (underscored) is new; matter in brackets [-] is old law to be omitted.

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under the Securities Investor Protection Act of 1970 and mandates membership of most United States registered broker-dealers.

(b) "Applicable agency" means a department or agency of this state established by law to regulate certain types of business activity in this state and persons engaged in such business, including the issuance of licenses or other types of authorization, that the attorney general and state comptroller determines would otherwise regulate a sandbox participant if the person were not a regulatory sandbox participant.

(c) "Consumer" means a person that purchases or otherwise enters into a transaction or agreement to receive a financial technology product or service that is being tested by a sandbox participant.

(d) "Financial products or services" means a product or service that requires licensure by the applicable agency or a product or service that includes a business model, delivery mechanism or element that may otherwise require a license or other authorization to act as a financial institution or enterprise or other entity that is regulated by the applicable agency.

(e) "Financial technology products or services" means a financial product or service with the use or incorporation of new or emerging technology or the reimagination of uses for existing technology to address a problem, provide a benefit or otherwise offer a product, service, business model or delivery mechanism that is not known by the attorney general to have a comparable widespread offering in this state. Such term shall include, but shall not be limited to, cryptocurrency business activity.

(f) "Cryptocurrency" means a digital currency which uses encryption techniques to regulate the generation of currency units and verify the transfer of funds, operating independently from a central bank.

(g) "Cryptocurrency business activity" means the conduct of any of the following types of activities involving New York or a New York resident:

(1) receiving cryptocurrency for transmission or transmitting cryptocurrency, except where the transaction is undertaken for non-financial purposes and does not involve the transfer of more than a nominal amount of cryptocurrency;

(2) storing, holding, or maintaining custody or control of cryptocurrency on behalf of others;

(3) buying and selling cryptocurrency as a customer business;

(4) performing exchange services of cryptocurrency as a customer business; or

(5) controlling, administering, or issuing a cryptocurrency.

(h) "Regulatory sandbox" means the program established by this article that allows a person to temporarily test financial technology products or services on a limited basis without otherwise being licensed or authorized to act under the laws of this state.

(i) "Sandbox participant" means a person whose application to participate in the regulatory sandbox is approved pursuant to this article.

(j) "Test" means to provide activity and services as allowed by this article.

§ 702. Reports; studies. (a) The attorney general and state comptroller shall publish annually a written report describing the results of the regulatory sandbox established pursuant to this article and the results of their studies conducted pursuant to subdivision (b) of this section.

(b) The attorney general and state comptroller shall study long term solutions to issues that arise from financial technology products or services, including, but not limited to:

(1) the use of third party depository and custodian services as auditors of financial technology products and services; and

(2) the use of the securities investor protection corporation to insure all financial technology products and services account holder's assets.

§ 703. Program purpose. The attorney general and state comptroller shall establish a regulatory sandbox in consultation with applicable agencies of this state to enable a person to obtain limited access to the market in this state to test financial technology products and services without obtaining a license or other authorization that otherwise may be required by law and without having to pay any fees associated with such license or authorization.

§ 704. Application process and requirements. (a) Any person may apply to enter the regulatory sandbox to test financial technology products or services.

(b) The attorney general and state comptroller shall create a joint office or coordinated process and shall accept and review each application for entry into the regulatory sandbox on a rolling basis.

(c) An application shall demonstrate that the applicant both:

(1) is an entity or individual that is subject to the jurisdiction of the attorney general and state comptroller through incorporation, residency, presence, agreement, or otherwise; and

(2) has established a location, whether physical or virtual, that is adequately accessible to the attorney general and state comptroller from which testing will be developed and performed and where all required records, documents and data will be maintained.

(d) Any person, corporation, partnership or other entity that already possesses a license or other authorization under state laws that regulate financial technology products or services shall file an application with the attorney general and state comptroller to test financial technology products or services within the regulatory sandbox.

(e) Applications shall contain sufficient information to demonstrate that an applicant has an adequate understanding of the financial technology product or service and a sufficient plan to test, monitor and assess the financial technology product or service while ensuring consumers are protected from a test's failure.

(f) Applicants shall contain the information required by a form developed and made publicly available by the attorney general and state comptroller. The information required by the form shall include, but shall not be limited to:

(1) relevant personal and contact information for the applicant, including full legal names, addresses, telephone numbers, e-mail addresses, website addresses and any other information that the attorney general and state comptroller deems necessary;

(2) disclosure of any criminal convictions of the applicant or key personnel, if any;

(3) a description of the financial technology products or services desired to be tested, including statements regarding all of the following:

(A) how a financial technology product or service is subject to regulation outside of the regulatory sandbox;

(B) how the financial technology product or service would benefit consumers;

(C) how the financial technology product or service is different from other products or services available in this state;

(D) what risks will confront consumers that use or purchase the financial technology product or service;

(E) how entering the regulatory sandbox would enable a successful test of the financial technology product or service;

(F) a description of the proposed testing plan, including estimated time periods for market entry, market exit and the pursuit of necessary licensure or authorization; and

(G) how the applicant will wind down the test and protect consumers if the test fails.

(g) A person shall file a separate application for each financial technology product or service sought to be tested.

(h) After the information required by subdivision (f) of this section is submitted, the attorney general and state comptroller may seek additional information that is deemed necessary. Not later than ninety days after an application is initially submitted, the attorney general and state comptroller shall notify the applicant as to whether the applicant is approved for entry into the regulatory sandbox. The attorney general and state comptroller and an applicant may mutually agree to extend the time period for the attorney general and state comptroller to determine whether an application is approved for entry into the regulatory sandbox.

(i) The attorney general and state comptroller may deny applicants at their discretion and such a denial shall not be an appealable agency action.

§ 705. Consultation with applicable agencies; admission authority; scope; insurance products; investment management. (a) (1) The attorney general and state comptroller shall consult with an applicable state agency before admitting a person into the regulatory sandbox. This consultation may include seeking information about:

(A) whether the applicable agency previously has either (i) issued a license or other authorization to the applicant, or (ii) investigated, sanctioned or pursued legal action against the applicant; and

(B) whether the applicant could obtain a license or other authorization from an applicable agency after exiting the regulatory sandbox.

(2) Notwithstanding paragraph one of this subdivision, the attorney general and state comptroller have the sole authority to make the final decision of whether to admit a person into the regulatory sandbox.

(b) If the attorney general and state comptroller approves an application for entry into the regulatory sandbox, the applicant is deemed a sandbox participant and both of the following shall apply:

(1) the sandbox participant has twenty-four months after the date of approval to test the cryptocurrency business activity described in the sandbox participant's application; and

(2) the attorney general and state comptroller shall issue the sandbox participant a registration number.

(c) Financial technology products or services that are provided within the regulatory sandbox are subject to the following restrictions:

(1) except as provided in subdivision (d) of this section, not more than ten thousand consumers may transact through or enter into an agreement to use the financial technology products or services;

(2) except as provided in subdivision (d) of this section, for a sandbox participant testing products or services as a money transmitter, individual transactions per consumer may not exceed ten thousand dollars and aggregate transactions per consumer may not exceed two million dollars over the course of the twenty-four months of the regulatory sandbox period;

(3) for sandbox participants testing products or services as a financing agency as defined in subdivision nine of section three hundred one of the personal property law, all of the following apply:

(A) section three hundred two of the personal property law;

(B) section three hundred three of the personal property law;

(C) section three hundred six of the personal property law;

(D) section three hundred eight of the personal property law; and

(E) section 9-601 of the uniform commercial code; and

(4) for sandbox participants testing products or services that provide investment management that is regulated each sandbox participant shall:

(A) make, maintain and preserve books and records in accordance with the requirements imposed on federal covered advisers under 17 CFR 275.204-2. The sandbox participant shall file with the state comptroller and the attorney general's office a copy of any notices or written undertakings required to be filed by federal covered advisers with the securities and exchange commission under 17 CFR 275.204-2; and

(B) comply with all requirements imposed on federal covered advisers under 17 CFR Part 275 with respect to:

(i) dishonest and unethical practices;

(ii) information required to be furnished to clients;

(iii) custody of client funds or securities; and

(iv) disclosure of financial and disciplinary information to clients.

(d) If a sandbox participant demonstrates adequate financial capitalization, risk management process and management oversight they may request the attorney general and state comptroller to allow either or both of the following:

(1) allow more than ten thousand consumers to transact through or enter into an agreement to use the financial technology product or service;

(2) for a sandbox participant testing products or services as a money transmitter, allow individual transactions per consumer to exceed ten thousand dollars and aggregate transactions per consumer to exceed two million dollars during the twenty-four month regulatory sandbox period.

(e) This section shall not restrict a sandbox participant who holds a license or other authorization in another jurisdiction from acting pursuant to and in accordance with such license or other authorization.

(f) A sandbox participant is deemed to possess an appropriate license under the laws of this state for any provision of federal law requiring state licensure or authorization.

(g) Except as otherwise provided in this article, a sandbox participant shall not be subject to state laws that regulate a financial product or service.

(h) The attorney general and state comptroller may determine that certain state laws that regulate financial products or services apply to a sandbox participant. If the attorney general and state comptroller make such determination and approve an application for entry into the regulatory sandbox, the attorney general and state comptroller shall notify the sandbox participant of the specific state regulatory laws that will apply to the sandbox participant.

(i) A sandbox participant may obtain, record, provide or maintain in electronic form any information, writing, signature, record or disclosure that is required by this article or may substitute any substantially similar equivalent information, writing, signature, record or disclosure that is approved by the attorney general and state comptroller.

§ 706. Consumer protection. (a) Before providing a financial technology product or service to consumers, a sandbox participant shall disclose to consumers all of the following:

(1) the name and contact information of the sandbox participant including the registration number provided by the attorney general and state comptroller;

(2) that the financial technology product or service is authorized pursuant to the regulatory sandbox and, if applicable, that the sandbox participant does not have a license or other authorization to generally provide products or services under state laws that regulate a financial product or service that is outside the regulatory sandbox;

(3) that the state does not endorse or recommend the financial technology product or service;

(4) that the financial technology product or service is a temporary test that may be discontinued at the end of the testing period, including the expected end date of the testing period; and

(5) that consumers may contact the attorney general and state comptroller to file complaints regarding the financial technology product or service being tested and provide the attorney general and state comptroller's telephone number and website address where complaints may be filed.

(b) The notifications prescribed in subdivision (a) of this section shall be provided to consumers in a clear and conspicuous form in accordance with New York state language access requirements. For internet or application-based financial technology products or services, consumers shall acknowledge receipt of such notifications before completion of a transaction.

(c) The attorney general and state comptroller may require that a sandbox participant make additional disclosures to consumers. When the attorney general and state comptroller approve an application for entry into the regulatory sandbox, the attorney general and state comptroller shall notify the sandbox participant of the additional disclosures.

§ 707. Exit requirements. (a) At least thirty days before the end of the twenty-four month regulatory sandbox testing period a sandbox participant must either:

(1) notify the attorney general and state comptroller that the sandbox participant will exit the regulatory sandbox, wind down its test and cease offering any financial technology products or services in the regulatory sandbox within sixty days after the twenty-four month testing period ends; or

(2) seek an extension to pursue a license or other authorization required by law.

(b) If the attorney general and state comptroller does not receive notification pursuant to subdivision (a) of this section, the regulatory sandbox testing period ends at the end of the twenty-four month testing period and the sandbox participant must immediately cease offering financial technology products or services.

(c) If a test includes offering financial technology products or services that require ongoing duties, the sandbox participant shall continue to fulfill those duties or arrange for another person to fulfill those duties after the date the sandbox participant exits the regulatory sandbox.

§ 708. Extensions. (a) A sandbox participant may request an extension of the regulatory sandbox testing period for the purpose of pursuing a license or other authorization required by law.

(b) The attorney general and state comptroller may grant or deny a request for an extension pursuant to subdivision (a) of this section by the end of the twenty-four month regulatory sandbox testing period. An extension pursuant to this subdivision is not effective for more than one year after the end of the regulatory sandbox testing period.

(c) A sandbox participant that obtains an extension pursuant to subdivision (b) of this section must provide the attorney general and state comptroller with a written report every three months that provides an update on efforts to obtain a license or other authorization, including any submitted applications for licensure or other authorization, rejected applications or issued licenses or other authorization.

§ 709. Auditing by third party depository or custodian services. All sandbox participants shall be audited by a third party depository or custodian service. Such third party depository or custodian service shall ensure that sandbox participants:

(a) have established and maintained a fund insuring a portion of their account holder's assets by the securities investor protection corporation which shall replace the bond system; and

(b) provide financial technology products or services in full compliance with this article.

§ 710. Recordkeeping and reporting requirements. (a) A sandbox participant must retain records, documents and data produced in the ordinary course of business regarding a financial technology product or service tested in the regulatory sandbox.

(b) If a financial technology product or service fails before the end of the testing period, the sandbox participant must notify the attorney general and state comptroller and report on actions taken to ensure consumers have not been harmed as a result of the financial technology products or services failure.

(c) A sandbox participant is subject to the requirements of section two hundred eight of the state technology law and shall notify the attorney general and state comptroller of any "breach of the security of the system" as defined in paragraph (b) of subdivision one of section two hundred eight of the state technology law.

§ 711. Records; disclosure; evidentiary effect. (a) Records that are submitted to or obtained by the attorney general and state comptroller in administering this article are not public records or open for inspection by the public.

(b) Records and information that are submitted or obtained pursuant to this article may be disclosed to any of the following:

(1) state and federal agencies;

(2) representatives of foreign countries that have regulatory or supervisory authority over the activities of the sandbox participant;

(3) a federal, state or county grand jury in response to a lawful subpoena; and

(4) the state auditor general for the purpose of conducting audits authorized by law.

(c) The attorney general and state comptroller and any applicable agency consulted by the attorney general and state comptroller are not liable for the disclosure of records, information or data received or obtained pursuant to this article.

(d) The disclosure pursuant to subdivision (b) of this section of a complaint or the results of an examination, inquiry or investigation of a sandbox participant does not make that information a public record and the sandbox participant or the sandbox participant's holding company may not disclose that information to the general public unless the disclo-

sure is required by law. A sandbox participant or the sandbox participant's holding company may not disclose, use or reference in any form comments, conclusions or results of an examination, inquiry or investigation in any type of communication to a customer or potential customer.

(e) This section shall not prevent the disclosure of information that is admissible as evidence in a civil or criminal proceeding brought by a state or federal law enforcement agency to enforce or prosecute civil or criminal violations of the law.

§ 712. Reporting requirements; monitoring; enforcement; agreements. (a) The attorney general and state comptroller may establish periodic reporting requirements on sandbox participants.

(b) The attorney general and state comptroller may seek records, documents and data from sandbox participants. On the attorney general and state comptroller's request, sandbox participants shall make such records, documents and data available for inspection by the attorney general and state comptroller.

(c) If the attorney general and state comptroller have reasonable cause to believe that a sandbox participant has engaged in, is engaging in or is about to engage in any practice or transaction that is in violation of this article or section three hundred fifty-two of the general business law, or that constitutes a violation of a state or federal criminal law, the attorney general and state comptroller may remove a sandbox participant from the regulatory sandbox or order a sandbox participant to exit the regulatory sandbox program.

(d) Removal from the regulatory sandbox shall not be an appealable agency action.

(e) Sandbox participants are subject to the consumer fraud provisions under article twenty-three-A of the general business law.

(f) The attorney general and state comptroller may enter into agreements with state, federal or foreign regulators that allow sandbox participants to operate in other jurisdictions and allow entities authorized to operate in other jurisdictions to be recognized as sandbox participants in this state.

§ 2. The banking law is amended by adding a new section 9-x to read as follows:

§ 9-x. Audit of financial technology products or services; prohibiting licensing fees. 1. The following terms, when used in this section, shall have the following meanings:

(a) "Financial technology products or services" means a financial product or service with the use or incorporation of new or emerging technology or the reimagination of uses for existing technology to address a problem, provide a benefit or otherwise offer a product, service, business model or delivery mechanism that is not known by the attorney general to have a comparable widespread offering in this state. Such term shall include, but shall not be limited to, cryptocurrency business activity.

(b) "Cryptocurrency business activity" means the conduct of any of the following types of activities involving New York or a New York resident:

(i) receiving cryptocurrency for transmission or transmitting cryptocurrency, except where the transaction is undertaken for non-financial purposes and does not involve the transfer of more than a nominal amount of cryptocurrency;

(ii) storing, holding, or maintaining custody or control of cryptocurrency on behalf of others;

(iii) buying and selling cryptocurrency as a customer business;

(iv) performing exchange services of cryptocurrency as a customer business; or

(v) controlling, administering, or issuing a cryptocurrency.

(c) "Cryptocurrency" means a digital currency which uses encryption techniques to regulate the generation of currency units and verify the transfer of funds, operating independently from a central bank.

2. Any person, corporation, partnership or other entity that provides financial technology products or services shall be audited by a public or private third party depository or custodian service. Such third party depository or custodian service shall:

(a) ensure that such person, corporation, partnership or other entity that provides financial technology products of services has established security protocols to safeguard them from theft;

(b) ensure that such person, corporation, partnership or other entity that provides financial technology products or services has established and maintained a fund insuring a portion of their account holder's assets by the securities investor protection corporation which shall replace the bond system; and

(c) regularly examine holdings of such person, corporation, partnership or other entity that provides financial technology products or services to ensure proper ownership of assets.

3. Notwithstanding any other law, rule or regulation, no person, corporation, partnership or other entity that provides financial technology products or services shall be required to pay a licensing fee in order to provide such financial technology products or services.

§ 3. This act shall take effect on the one hundred eightieth day after it shall have become a law and shall expire and be deemed repealed July 1, 2028; provided, however, that effective immediately, the addition, amendment and/or repeal of any rule or regulation necessary for the implementation of this act on its effective date are authorized to be made and completed on or before such effective date.