Do You Venmo? FTC Spotlight on Peer-to-Peer Payments and Crowdfunding

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The FTC recently examined peer-to-peer (P2P) payment systems and crowdfunding in the second forum of its FinTech series. P2P payment systems are online services that allow consumers to share money electronically. These platforms enable the immediate transfer of money between consumers, typically for free or for a small fee. In the panel discussion of P2P payments, the following themes emerged: P2P payments have been transformational to the online payment industry and have changed consumer expectations about how money is being moved; these platforms likely will be disproportionately targeted by sophisticated hackers; and there are high barriers to entry into this market, in terms of cost and regulatory risk.

Crowdfunding is the process by which companies and individuals raise money from the public to fund new products, projects, or individual needs. Panelists discussed the responsibility platforms bear to shape consumer understanding of crowdfunding campaigns through adequate disclosure and communication.

The following expands on these themes and provides key takeaways from the forum:

P2P Payments as Transformational

Panelists (see list here) described the consumer benefits of P2P payments as enormous. The benefits go beyond splitting the dinner check or paying the babysitter with a few taps on a smart phone. P2P payments have expanded financial access to underserved communities, in particular, to underbanked and non-banked consumers. For example, P2P platforms enable instantaneous remittance payments or the wiring of funds, and remove obstacles in conventional banking such as delayed payment transfers and overdrafts.

And P2P platforms are not just a thing for millennials. Studies report that while millennials are conducting approximately 11 transactions a year, 45-54 year olds are conducting about 4 transactions and the over 65 crowd about 3.[1]

Fraud Risk

P2P payment systems collect more consumer data beyond the traditional credit card services. Therefore, panelists believe these platforms may be disproportionately targeted by sophisticated hackers. As one panelist aptly noted: “The mode is new, but the scams are old.” One positive attribute about Fintech companies is their typical approach to data security: they are extremely good at authentication and many view themselves first as security companies. Indeed, the weakest security points in P2P payments may not be in the platform, but the consumers using the services and security vulnerabilities in their devices (for more on IoT security, see here). In response, panelists noted the importance of appropriate and reasonable data security protocols to protect consumer data in this space.

Regulatory Risk

Panelists noted the high barriers to entry into this market. This is due to the various state licensing requirements for money transmission, and to the consumer protection issues raised by this type of mobile platform. Depending on the platform type, different sets of regulation may apply, including the following:

- Banking regulations and money transfer regulations;
- Electronic Funds Transfer (EFT) Act, Reg E, requiring that financial institutions and any third party involved in EFT services disclose specific information to consumers before engaging in any transactions;
- Truth in Lending Act and Reg Z, requiring that creditors disclose clearly and conspicuously in writing the terms of the legal obligation between the parties;
- Section 5, Federal Trade Commission Act, prohibition against unfair or deceptive acts and practices; and
- Dodd-Frank's prohibition against unfair, deceptive, and abusive acts and practices.

In addition, panelists noted the applicability of the new prepaid rulemaking issued by the CFPB. The new rule applies specific federal consumer protections to broad swaths of the prepaid market for the first time. It covers traditional prepaid cards, including general purpose reloadable cards, and extends to newer platforms such as mobile wallets and P2P platforms. The regulations require adequate disclosure, liability protection, among other things. See here for more information on this rulemaking.

There was discussion among the panelists on how to communicate effectively to consumers the information collected and stored by these platform. As a cautionary tale, panelists noted the Texas Attorney General action in May 2016 against PayPal involving its Venmo mobile app. The app allegedly failed to clearly disclose how consumers' transactions and interactions with other users would be shared, and misrepresented that communications from Venmo were actually from particular Venmo users. As a result, consumers may have publically exposed private information regarding their payments.

Crowdfunding

Crowdfunding is an evolving method of raising capital that has been used to raise funds through the Internet for a variety of projects.[2]

There are four basic types of crowdfunding: donation-based (e.g., GoFundMe, etc.); rewards-based (e.g., Kickstarter); equity-based (e.g., Crowdfunder.com); and debt-based (e.g., LendingClub). Equity and debt-based crowdfunding offerings are considered securities and subject to regulation by the SEC.[3] Donation and rewards-based crowdfunding generally are not regulated. Hence the FTC's heightened interest in ensuring these sites are not engaging in unfair or deceptive acts or practices in violation of Section 5 of the FTC Act.

Indeed, the FTC settled its first case in June 2015 against a creator of a crowdfunding project, Erik

Chevalier (The Forking Path). Chevalier allegedly raised money from consumers to produce a board game through a Kickstarter campaign, but instead used most of the funds on himself and refused to provide refunds to his backers. Chevalier was fined approximately $112,000 and is prohibited from making misrepresentations about any future crowdfunding campaign.

Panelists discussed the import of the FTC’s settlement, in particular, the responsibility that crowdfunding platforms bear to shape consumer understanding and to monitor creators for fraud. Panelists agreed there was a role for both regulators to pursue fraud and for industry self-regulation to adopt best practices.

FinTech companies face high barriers to entry, an uncertain regulatory environment, and increased privacy and data security concerns. But the benefits to consumers of these types of novel platforms are enormous. P2P payments expand financial services to underserved communities; creators of successful crowdfunding projects may have access to venture capital previously unavailable to them. Regulators therefore seek to balance technological innovation with consumer protection directives, in particular, to ensure all players keep their promises, tell consumers the truth, and provide adequate disclosures.

1. Javelin LLC, *P2P Payments in 2015: Market Sizing and Evaluation of P2P* (Dec. 2015).
2. U.S. Securities & Exc. Comm’n, *SEC Adopts Rules to Permit Crowdfunding* (Oct. 30, 2015).
3. The SEC adopted Regulation Crowdfunding in October 2015 to enable individuals to purchase securities in crowdfunding offerings subject to certain limits, require companies to disclose certain information about their business and securities offering, and create a regulatory framework for the intermediaries facilitating crowdfunding transactions.