FIRST IN THE NATION: ARIZONA’S
REGULATORY SANDBOX†

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Consumer protection regulators have a dual mandate to protect consumers by preventing both fraud and market distortions. Regulatory sandboxes have the potential to mitigate the market distortions created by regulatory barriers to entry and regulatory uncertainty, while maintaining consumer protection through monitoring and enhanced enforcement capabilities. Regulatory sandboxes have been utilized around the world to facilitate innovative financial products and services. Arizona has created the United States’ first regulatory sandbox program. This article identifies the need for regulatory sandboxes, describes sandboxes around the world, discusses the specific details of Arizona’s sandbox, and explains how Arizona is leading the way for regulatory innovation in the United States.

I. INTRODUCTION–IMPORTANCE OF INNOVATION FOR CONSUMERS AND STATES

A Financial Technology (“FinTech”) regulatory sandbox’s value proposition essentially involves a trade where a sandbox participant obtains reduced barriers to entry into a regulated market in exchange for limited access to that market. When properly administered, sandboxes promote regulators’ dual mandate to protect consumers by preventing fraud and reducing market

† The views expressed herein are solely those of the authors and do not necessarily represent those of the Arizona Attorney General or the State of Arizona.

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distortions. This article identifies the advantages of regulatory sandboxes in facilitating innovation that benefits consumers and states, and explains Arizona’s FinTech Sandbox in greater detail.

a. Regulators’ Dual Mandate

Regulators’ dual mandate to prevent both fraud and market distortions is evident from the history of modern consumer protection law. The first Federal Trade Commission (“FTC”) consumer fraud actions targeted fraud because it distorted the market by benefiting fraudsters at the expense of honest businesses.\(^1\) Moreover, antitrust law inherently focuses on combating market distortions,\(^2\) and, as demonstrated by the FTC’s litigation against the North Carolina State Board of Dental Examiners, regulators recently have expanded their scope to include identifying and addressing distortions produced by state-established entities.\(^3\)

This dual mandate recognizes important truths about the advantages and limitations of markets. From the consumer perspective, the mere existence of dynamic markets provides a core consumer protection: competitive options.\(^4\) Such options protect consumers by incentivizing existing businesses to improve services or reduce prices (or both) to avoid losing customers.\(^5\) The history of financial services contains many examples of this phenomenon attributable to new technology, including the increased convenience

\[^1\] See FTC v. Winsted Hosiery Co., 258 U.S. 483, 494 (1922) (“The honest manufacturer's business may suffer, not merely through a competitor's deceiving his direct customer, the retailer, but also through the competitor's putting into the hands of the retailer an unlawful instrument, which enables the retailer to increase his own sales of the dishonest goods, thereby lessening the market for the honest product.”); FTC v. Raladam Co., 283 U.S. 643, 649, (1931) (“[T]he trader whose methods are assailed as unfair must have present or potential rivals in trade whose business will be, or is likely to be, lessened or otherwise injured.”).

\[^2\] See Robert H. Lande, Consumer Choice as the Ultimate Goal of Antitrust, 62 U. PITT. L. REV. 503 (2001) (“The antitrust laws are intended to ensure that the marketplace remains competitive so that worthwhile options are produced and made available to consumers, and this range of options is not to be significantly impaired or distorted by anticompetitive practices.”).


\[^5\] Sam D. Johnson & A. Michael Ferrill, Defining Competition: Economic Analysis and Antitrust Decisionmaking, 36 BAYLOR L. REV. 583, 591 (1984) (arguing that businesses can only raise prices through more efficient production techniques or better products).
of mobile banking and the higher interest rates from online savings accounts.\footnote{Andrew Palmer, In Defense of Financial Innovation, 94 FOREIGN AFF. 66, 70 (2015).}


But even competitive markets, for all their advantages, will never eliminate the need for regulators to combat fraud. Fraud’s short-term benefits are significant, and accordingly regulators must impose serious consequences that make fraudulent actions unprofitable and unattractive. The United States provides numerous avenues for preventing and redressing fraud in financial services, including fifty state licensing and enforcement regimes and at least five federal agencies.\footnote{Elizabeth F. Brown, E Pluribus Unum-Out of Many, One: Why the United States Needs A Single Financial Services Agency, 14 U. MIAMI BUS. L. REV. 1, 5 (2005).}

Regulatory sandboxes present the potential to retain the benefits of enforcement authority, while reducing distortions caused by some regulations.

b. Regulatory Barriers to Entry

Licensing and compliance costs create significant barriers to market entry in the United States. A 2017 KPMG report noted that
“[t]he myriad state, federal and, for some banks, international financial regulations and reporting requirements [have] led many financial institutions to become overwhelmed by the amount of effort and budget required to be in compliance.”12 This burden is imposed primarily at the federal level. At the end of 2017, the Code of Federal Regulations (“CFR”) contained at least 156,000 different restrictions that require or prohibit some activity in the financial services sector.13 Contrast the scale of that burden with a state such as Arizona, where state regulations impose approximately 5,200 restrictions in Title 6, the title governing most financial services.14

In addition to the sheer number of requirements that may apply to market entrants in any given state, launching a financial services business in the United States multiplies that problem by fifty. The requirement to comply with over 115 different licensing and compliance regimes significantly increases the delay and expense of launching new products in the United States.15

c. Encouraging Increased Venture Capital Investment

High costs from barriers to entry and compliance burdens disfavor new entrants and necessarily require any such entrants to obtain significant levels of venture capital to more easily absorb these costs.16 Because capital is concentrated in a small number of

13 Patrick A. McLaughlin & Oliver Sherouse, QuantGov—A Policy Analytics Platform: RegData 3.1 3-Digit Industry Summary, MERCATUS CTR. (2017), available at https://s3.amazonaws.com/quantgov-datasets/regdata/RegData3.1/extracts/cfr_naiics07-3digit_extract.csv (This figure was calculated by adding the restrictions associated with the North American Industry Classification System numbers of 521, 522, 523, 524, and 525 within the dataset).
states, the need to obtain such capital to account for high compliance costs necessarily disadvantages the rest of the country from being a viable option for new entrants. Venture capital (“VC”) investment is heavily concentrated in New York, California, and Massachusetts. Together, these three states accounted for 77% of venture capital investment in the United States in 2016. These numbers are not just a function of larger investments—the same three states also obtained 64% of deals in 2016. These empirical findings appear to validate venture capitalists’ anecdotal rule: “If a start-up company . . . is not within a 20-minute drive of the venture firm’s offices, it will not be funded.”

If new entrants to financial services face high costs in acquiring access to significant levels of venture capital, and that capital is concentrated in three states, then the remaining forty-seven states and their entrepreneurs may lose out on the opportunity to build a FinTech ecosystem. On the other hand, a state that meaningfully lowers the cost of innovation (while protecting consumers) likely would benefit its own entrepreneurs and attract innovators from other states or overseas. The concentration of these enterprises and the benefit of live testing within a sandbox may give venture capital a reason to leave its narrow ambit on the coasts to create a more diverse investment portfolio.

Increased investment across a broader portion of the country is much needed given the geographic concentration of the economic recovery since 2008. Between 2010 and 2014, only twenty counties, comprising 17% of the nation’s population, have accounted for half

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18 Ksiaikiewicz, supra note 17.


of the net increase in business establishments. Significant
differences are reflected in per capita GDP as well. In 2017,
Massachusetts, New York, and California respectively had over
$66,000, $65,000, and $60,000 in per capita GDP. By comparison,
eleven states (Florida, Montana, Arizona, Maine, Kentucky, South
Carolina, Alabama, West Virginia, Arkansas, Idaho, and
Mississippi) had less than $40,000.

While the precise economic effect of increased venture
capital investment is disputed, anecdotal evidence and some
statistical surveys demonstrate its significance. For example, even
though only .05% of startups receive VC funding, since 1979, 43%
of publicly traded companies have been backed by VC.

Furthermore, researchers at the Martin Prosperity Institute found
that increasing the supply of VC increases business start-ups,
employment, and income levels. Given the importance of the
economic issues at stake, states would do well to look outside the
United States for successful strategies to attract increased
investment. One of those strategies is a regulatory sandbox.

II. REGULATORY SANDBOXES ABROAD

Countries abroad have recognized the opportunity
regulatory sandboxes present. Three years ago, the United Kingdom
proposed the world’s first regulatory sandbox. The U.K. sandbox

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25 Ilya Strebualev & Will Gornall, How Much Does Venture Capital Drive the
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economy.
26 Sampsamila & Olav Sorenson, Venture Capital, Entrepreneurship, and
27 U.K. FIN. CONDUCT AUTH., REGULATORY SANDBOX (2015), available at
admits participants in periodic “cohorts.” Companies in the cohorts admitted thus far have ranged from small start-ups to established banks such as HSBC and Lloyds Banking Group. Ideas tested have varied in subject matter, including blockchain, insurance, money transfer, consumer-focused financial management apps, and consumer loans. The first year was a success as “the majority of tests have developed as planned towards meeting their objectives and the [U.K. Financial Conduct Authority] currently expects most firms to take forward their propositions to market.”28 Around 90% of firms who tested during the first year are continuing to a wider market launch.29 At least 40% of products tested in the first cohort received investment during or following the sandbox tests.30 As of this writing, the second cohort is currently in the sandbox and the Financial Conduct Authority (“FCA”) has accepted 18 firms into the third cohort.31 Interestingly, the sandbox’s creation corresponded with an investment increase in UK FinTech firms from $140 million in the first quarter of 2016 to $375 million in the first quarter of 2017.32

In the United Arab Emirates, the Abu Dhabi Global Market (“ADGM”) administers a regulatory sandbox called the “RegLab.”33 ADGM utilizes a “blank-sheet” approach, in which companies begin with no rules or regulations.34 The ADGM then formulates a customized set of rules depending on the business model,

30 Id. at 6.
technology deployed, and risk-profile of the company. The ADGM determines which existing regulations apply to the company and then issues waivers or modifications for the rules that do not apply. Regulators set exposure limits, boundaries, and restrictions to protect consumers in the sandbox. The rules can change at different stages in the sandbox to mitigate risk as appropriate. Companies have two years to develop, test, and launch their products. Companies with successful results may receive full authorization from the existing supervisory regime and deploy their innovation on a wider scale.

As of this writing, over twenty-seven other countries have created or are formulating a regulatory sandbox. Australia, Bahrain, Canada, Hong Kong, Malaysia, the Netherlands, Singapore, Thailand, the United Arab Emirates, and the United Kingdom all have operational sandboxes. Brazil, China, India, Japan, Jordan, Kenya, Mexico, the Republic of Korea, Russia, Sweden, Switzerland, Taiwan, and Turkey have all officially announced sandboxes. The lack of government support for a sandbox within the United States has been cited as a dampening factor in FinTech growth. Arizona has paved the way for utilizing sandboxes within the United States.

III. ARIZONA REGULATORY SANDBOX PROGRAM

In March 2018, legislation initiated by Arizona Attorney General Mark Brnovich, sponsored by State Representative Jeff

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35 Id. at 5.
36 Id.
37 Id.
38 Id.
39 Id. at 6.
40 Id. at 6-12.
42 Jenik & Lauer, supra note 41 at 11.
43 Id.
Weninger, was signed into law by Governor Doug Ducey, creating the first FinTech regulatory sandbox in the United States.\textsuperscript{45} Effective August 3, 2018, the Arizona Attorney General’s Office will administer the Sandbox.

The Arizona Sandbox ("Sandbox") lowers barriers to entry primarily for three broad categories of FinTech: money transmission, consumer lending, and investment advice. Other products that would otherwise be regulated by the Department of Financial Institutions, such as escrow agents, also may be considered. Regulations outside the scope of the Sandbox remain in effect. As a result, insurance is not eligible for exemptions.\textsuperscript{46} While state securities regulation is also outside of the Sandbox, some applicants may choose to use the Sandbox in conjunction with Arizona’s new intrastate offering legislation that allows low-cost offerings up to $5 million and exempts in-state initial coin offerings meeting certain criteria.\textsuperscript{47} Each application for entry into the Sandbox must be for an innovative financial product\textsuperscript{48} or service, which is broadly defined as:

\begin{quote}
[T]he 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.\textsuperscript{49}
\end{quote}

After completing the streamlined application process detailed below, Sandbox participants can test their product over a two-year period with up to 10,000 Arizona consumers. If a participant can demonstrate adequate capitalization and risk management, up to 17,500 Arizona consumers may participate in a

\textsuperscript{46} To be eligible for the Arizona Sandbox, a product or service must fall within the category of “financial product[s] or service[s],” which are defined as “product[s] or service[s] that require licensure under Title 6 or Title 44, Chapter 2.1 or 13” \textit{See} ARIZ. REV. STAT. ANN. § 41-5601(3) (2018).
\textsuperscript{47} H.B. 2601, 53d Leg., 2d Sess. (Ariz. 2018).
\textsuperscript{48} Note 47 defines financial products and services. Innovative financial products or services include an innovation. \textit{ARIZ. REV. STAT. ANN. § 41-5601(5)}.
\textsuperscript{49} \textit{Id.} § 41-5601(4).
test. Additionally, participants can obtain up to a year-long extension to gain licensure before exiting the Sandbox.

d. Application Process

Entering the Sandbox requires applying to the Arizona Attorney General’s Office (“Attorney General’s Office”), including a $500 application fee. Each application must seek to test a single innovative financial product or service. The Attorney General’s Office will accept applications at any time and provide a decision regarding applications within 90 days of receipt.

The law requires the Attorney General’s Office to review two broad factors in evaluating applications. First, applicants must anticipate risks for consumer harm, and have a plan and the ability to make consumers whole if the risk materializes. Second, applicants must demonstrate thorough knowledge of the product or service to be tested. This includes an understanding of the product, showing that resources are in place to ensure a successful test, and articulating how the success of the product will be determined. Here, applicants show that an idea is more than just a thought; it is ready to be realized in an active market.

To these ends, the application consists of three main parts: (i) information about the applicant; (ii) information about the innovation being tested; and (iii) information about the testing plan. The application defines certain key terms, such as “key personnel,” to give businesses guidance in answering the questions. If necessary, the Attorney General’s Office may ask applicants additional questions to make an informed decision.

First, applicants must provide descriptive information about the business. This includes contact information, the full legal names of the applicant’s key personnel, the type of technology the applicant is seeking to test, how the applicant is subject to Arizona’s jurisdiction, what other authorizations the applicant already has, how the applicant plans to partner with other entities during the test,

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50 Id. § 41-5605(C).
51 Id. § 41-5603(H).
52 Id. §§ 41-5603(F)(3)(d), (g).
53 Id. § 41-5603(E).
54 Id. § 41-5603.
55 The Attorney General’s Office has some latitude in developing the form and requesting information it deems necessary. Id. §§ 41-5603(F); 41-5603(F)(1).
56 Id. § 41-5603(I).
57 See generally id. § 41-5603(F).
and whether any of the key personnel or associated entities have ever been prosecuted.\textsuperscript{58}

Second, applicants must explain the innovation.\textsuperscript{59} Applicants must discuss the stage of development and include any business plans, white papers, or other relevant materials. Applicants must demonstrate sufficient understanding of the technology underlying the innovation being tested, a plan for testing, and a methodology of monitoring the test while securing proper safeguards for consumers.\textsuperscript{60} Applicants must discuss how they anticipate being regulated outside of the Sandbox.\textsuperscript{61} Applicants also must discuss how the innovation compares to what is already happening in the market—for example, why the idea is innovative; who the applicant will compete against; and what benefits the innovation provides to consumers.\textsuperscript{62} Answers to these questions inform the broader context against which the Attorney General’s Office will evaluate the innovation.\textsuperscript{63}

Third, applicants must describe a testing plan.\textsuperscript{64} Identifying and mitigating risks to consumers is one of the most important aspects of proposing a serious testing plan that the Attorney General’s Office can accept as Sandbox-appropriate. The applicant must show a risk mitigation strategy commensurate with risks. For example, a proposed test aimed at reaching up to 17,500 consumers, the maximum possible under the Sandbox law, must include information showing that safeguards are in place that can adequately address problems that may be encountered by a large number of potential consumers.\textsuperscript{65} Conversely, an applicant restricting a product to substantially fewer consumers may allow for a more dynamic test where additional safeguards, if needed, could be identified and implemented while testing is underway.

\textsuperscript{58} Id.
\textsuperscript{59} Id.
\textsuperscript{60} Id. § 41-5603(F)(3)(f)-(g).
\textsuperscript{61} Id. § 41-5603(F)(3)(a).
\textsuperscript{62} Id. § 41-5603(F)(3)(c).
\textsuperscript{63} Id. §§ 41-5603(F)(3)(b); 41-5603(F)(3)(c).
\textsuperscript{64} Id. § 41-5603(F)(3)(f).
\textsuperscript{65} Applicants may seek to provide their product or service to up to 17,500 consumers. If the applicant is a money transmitter, then the transaction limit may be raised to $15,000 per consumer and in the aggregate $50,000 per consumer. See id. § 41-5605(C).
Proposed testing plans also should include estimated milestones, both in terms of time and indicators of success. For example, an applicant may outline a quarterly goal for the number of consumers that are engaged with the product. Applicants may include the licensure extension period in their original application, and the Attorney General’s Office will consider such incorporation on a case-by-case basis. Extensions will only be granted to obtain licensure.

Finally, successful applications must describe the wind-down phase of the testing plan. Applicants must think through an exit plan for at least three different scenarios: (i) a test’s failure, i.e., the test must cease and consumers be made whole; (ii) the business obtains or is in the process of obtaining state licensure to continue its business outside of the Sandbox during or after the two year testing period; and (iii) the two-year testing period expires and the participant does not obtain the requisite authorization. In each scenario, exit plans should focus on consumers who may be affected. Applicants should consider developing further contingency plans to prevent unforeseen circumstances, such as in the case of a data breach.

This streamlined application process differs from the typical licensure application process through NMLS. Typical licensure applications require similar types of information but in much greater detail. For example, while Sandbox applicants may provide financial statements as supporting documents in the Sandbox application, the Arizona Department of Financial Institutions’ (“AZ DFI”) application requires audited financial statements. Additionally, the AZ DFI application process can require several different applications, such as an application for each branch

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66 Id. § 41-5603(F)(3)(f).
67 Id. § 41-5607(A)(2).
68 See generally id. § 41-5607.
69 See id. § 41-5609(C).
71 Id. at 104.
72 Depending on the license a person is seeking, there are different requirements. For example, ARIZ. REV. STAT. ANN. § 6-186 requires banks to at least annually perform audits to maintain licensure.
location and each manager of the company. The Sandbox application does not impose these same burdens.

e. Consumer Protection

The Sandbox retains key consumer protections, and provides the Attorney General’s Office enhanced enforcement tools. Sandbox participants will be subject to Arizona’s consumer protection laws, including the state Consumer Fraud Act and interest rate caps for consumer loans. Moreover, the Attorney General’s Office retains all of its powers under Arizona law to protect consumers, prevent fraud, and enforce the law.

Along these lines, Sandbox participants may be removed from the Sandbox upon a reasonable cause determination by the Attorney General’s Office that a participant is not following the law or is circumventing its obligations within the Sandbox. And participants that engage in deceptive acts or practices are subject to the full scope of enforcement available to the Attorney General’s Office for any other person doing business in Arizona.

Additionally, the law imposes new requirements on transaction size and the number of consumers that can participate in a test. If the Participant is deemed to be testing a consumer lending product or service, loans will be limited to $15,000 per loan and $50,000 per consumer. The interest rate caps established by state law still apply—36% for the first $3,000 of the principal and 24% on any principal amount above $3,000. If a variable interest rate is linked to an index, the interest rate cannot increase or decrease more than 3% in any twelve-month span. Additionally, the interest rate cannot vary by more than 7%, above or below the original interest rate, over the life of the loan.

In addition to interest, current state law related to finance charges also apply to Sandbox participants. These charges can

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74 Id. § 41-5611.
75 Id. § 41-5605(B)(3); § 6-601(6) defines consumer lender loans as “consumer loans, consumer revolving loans and home equity revolving loans.”
76 Id. § 41-5611.
77 Id. § 41-5611(C).
78 See, e.g., id. § 41-5611(E).
79 Id. § 41-5605(B)(3).
80 Id.
81 Id. § 6-632(A).
82 Id. § 6-632(C).
83 Id.
include delinquency charges up to 5% of unpaid installment, third-party costs, and costs arising from perfecting liens and security interests.\(^\text{84}\) Additionally, lenders may charge loan origination fees, but the fees are capped at $150.\(^\text{85}\) Lenders cannot charge loan origination fees for renegotiations of credit transactions culminated within the past year, or if the lender charges prepaid finance charges.\(^\text{86}\) Lenders may charge for costs that arise in the normal course of collecting debt, which may be court costs or attorney fees. Allowable charges are set by statute.\(^\text{87}\) Thus, status as a Sandbox participant does not allow for avoiding existing consumer safeguards regarding finance charges.

Similarly, other specific laws regarding consumer lending, money transmission, sales finance companies, and investment management are incorporated into the Sandbox to protect consumers.\(^\text{88}\) For example, sales finance companies—businesses that sell motor vehicles with one or more deferred payments—still must comply with default rights and include certain contract terms and provisions as provided in state law.\(^\text{89}\) In another example, investment management businesses remain subject to the special anti-fraud statutory provision applicable to such businesses.\(^\text{90}\)

By incorporating these state law provisions, the Sandbox maintains important consumer protections while also lowering the barriers to entry and regulatory burden for participants. And the Arizona Attorney General’s Office possesses significant discretion to impose the requirements of additional state laws and regulations as may be necessary.\(^\text{91}\)

Consumer protection also will be accomplished in the Sandbox through monitoring by the Arizona Attorney General’s Office during testing. Once in the Sandbox, participants will be subject to some periodic monitoring with the goal of ascertaining a

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\(^{84}\) Id. § 6-635(A).
\(^{85}\) Id. § 6-635(A)(4). The cap on loan origination fees is either 5% of the principal or, for revolving loans, credit limit, but in no event shall the fee be more than $150.
\(^{86}\) Prepaid finance charges, as used in this section, refer to loans of at least $5,000 secured by the consumer’s principal residence. These finance charges are limited to 4% of the principal amount. See id. § 6-635(A)(4)(b).
\(^{87}\) Id. § 6-632 (incorporated by reference in A.R.S. § 41-5605(B)(3)(b)).
\(^{88}\) See id. § 41-5605(B)(4)-(6).
\(^{89}\) Id. §§ 41-5605(B), 47-9601.
\(^{90}\) Id. § 44-3241.
\(^{91}\) Id. § 41-5605(G).
test’s progress as well as whether consumers are being properly informed about the product or service they are using. To facilitate this, sandbox participants will be required to retain certain records produced in the ordinary course of business while conducting a test.92 These proactive regulatory measures are in addition to a participant’s duty to keep the Attorney General’s Office appraised of failing tests and mitigating actions taken by a participant.

These actions collectively demonstrate that lowering regulatory barriers to entry do not require corresponding reductions in consumer protection. Indeed, the Sandbox provides the Attorney General’s Office with significant authority to act quickly and decisively to protect consumers. In addition, the Sandbox allows the Attorney General’s Office to foster a close working relationship with participants that, ideally, will allow participants to leverage the Sandbox’s flexibility into fully operational innovative products and services that provide significant benefit to consumers in the marketplace.

IV. REGULATORY COORDINATION

In a global economy, realizing a sandbox’s full potential requires connecting with other markets and potentially coordinating with regulators in various jurisdictions. The Arizona Sandbox anticipated this by granting the Attorney General’s Office authority to enter into agreements with other states, federal agencies, and foreign regulators that may allow Sandbox participants access to markets beyond Arizona.93 The Arizona Attorney General’s Office already has begun engaging other regulators to this end.

Coordination between regulators will be a necessary component to ensuring regulatory systems keep pace with innovation. Within the United States especially, the federal system of overlapping regulatory jurisdictions requires coordination between domestic regulators to provide reasonable levels of certainty to state sandbox participants. Even as federal regulators continue to contemplate whether a sandbox model will work within their jurisdictions,94 federal agencies nevertheless can coordinate with state regulators through exemptions to achieve similar ends. As

92 Id. § 41-5609(A).
93 Id. § 41-5611(F).
Arizona Attorney General Mark Brnovich has noted, federal agencies have authority to issue rules exempting entities within state sandboxes from federal regulations. As established in statute and affirmed by the courts, federal agencies have the power to exempt classes of persons or transactions from certain statutory provisions, as well as regulations an agency promulgates and enforces. As most relevant to FinTech, the Bureau of Consumer Financial Protection (“BCFP”), Securities and Exchange Commission (“SEC”), Commodity and Futures Trading Commission (“CFTC”), Department of the Treasury, and the Federal Trade Commission (“FTC”) all possess specific authority to create a method for granting exemptions. Given the strong consumer protection focus of sandbox programs like Arizona’s, exemptions from federal regulations could be granted when sandbox participants remain subject to state consumer fraud statutes. Without such exemptions, state sandbox efforts will be hampered by the need to comply with potentially redundant federal regulatory structures.

V. CONCLUSION

Innovative FinTech is hampered in the United States by the patchwork of regulatory barriers and legal uncertainty it faces. Regulatory sandboxes offer one way to lower the regulatory burden associated with successfully navigating this patchwork system. As many other countries have recognized, sandbox programs provide an avenue for regulators to fulfill their consumer protection mission

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96 See United States v. Allegheny-Ludlum Steel Corp., 406 U.S. 742, 755 (1972) (“It is well established that an agency's authority to proceed . . . by means of rules of general application entails a concomitant authority to provide exemption procedures in order to allow for special circumstances.”); see also In re Permi Basin Area Rate Cases, 390 U.S. 747, 784-86 (1968).
97 See 12 U.S.C. § 5512(b)(3)(A) (2016) (CFPB may “exempt any class of covered persons, service providers, or consumer financial products or services, from any provision of [Title 12 of the United States Code], or from any rule issued under [Title 12], as the Bureau determines necessary or appropriate to carry out the purposes and objectives of [Title 12]”); 15 U.S.C. § 1604(f)(1) (2015) (allowing for exemptions from the Truth In Lending Act); id. § 1604(f)(1) (permitting the CFPB to issue such exemptions via rulemaking).
98 Id. §§ 77z-3, 78mm, 80a-6(c), 80b-6a.
99 7 U.S.C §§ 6(c), 6a(a)(7) (2016).
100 31 C.F.R. § 1010.970(a) (2016).
while also avoiding market distortion. In addition to promoting innovation, sandboxes also provide regulators with an invaluable education into cutting-edge ideas that will find their way into the marketplace. Consumers and businesses alike benefit from sandbox programs that foster innovation by giving such products and services a real chance of becoming available in the marketplace. By creating the first sandbox program in the United States, Arizona is leading the way in facilitating FinTech in American markets.