

DEPARTMENT OF BUSINESS OVERSIGHT*Ensuring a Fair and Secure Financial Services Marketplace for all Californians***Jan Lynn Owen****Commissioner of Business Oversight**

October 4, 2018

Re: _____ – Opinion Request

Dear _____:

Thank you for your letters to the Department of Business Oversight dated June 6, 2018 and August 28, 2018. You have requested a determination that the payment processing services conducted by _____ (“_____”) do not constitute money transmission. In the alternative, you have requested a determination that _____’s payment processing services meet the requirements of the agent of payee exemption¹ in the Money Transmission Act (“MTA”).

BACKGROUND

_____ is a Delaware corporation with a principal place of business in New York and offices in Delaware. _____ provides payment processing services to businesses that sell goods and services online. To provide its payment processing services, _____ enters into Merchant Services Agreements with businesses and processing agreements with card companies.² The payment processing services involve the following steps: (1) When a purchaser seeks to make an online purchase via credit or debit card, _____ requests a purchase authorization from the relevant card company. If authorization is granted, _____ communicates the authorization to the business selling the goods or services. (2) _____ submits required data about the purchase to the card company. (3) _____ settles the payment owed to the business (collectively, “Settlement Activities”).

¹ Fin. Code, § 2010, subd. (l).

² Card companies include _____, _____, and _____.

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In connection with the Settlement Activities, a card company may use _____'s platform to transfer funds to businesses. You provided a flow of funds chart that shows funds flowing from a consumer's bank account to the card company's bank account, the card company's bank account to _____'s bank account, and _____'s bank account to the business's bank account.

If a consumer cancels a purchase, a chargeback occurs requiring _____ to pay the purchase price back to the card company and collect the same amount from the business, less any fee paid by the business to _____. To mitigate credit exposure, _____ may require a business to establish and maintain a minimum balance in a reserve account controlled by _____. If a business fails to reimburse _____ for a chargeback, _____ may apply reserve account funds against the loss.

MONEY TRANSMISSION ACT

The MTA prohibits a person from engaging in the business of money transmission in California, unless the person is licensed or exempt from licensure or is an agent of a person licensed or exempt from licensure.³

A. Receiving Money for Transmission

Financial Code section 2003, subdivision (q)(3) defines "money transmission" to include receiving money for transmission. Financial Code section 2003, subdivision (u) defines "receiving money for transmission" to mean receiving money or monetary value in the United States for transmission within or outside the United States by electronic or other means. _____ receives money in an Illinois bank account for transfer to business merchant bank accounts. This constitutes receiving money for transmission pursuant to Financial Code section 2003, subdivision (u).

Financial Code section 2003, subdivision (k) defines "in California" to mean physically located in California, or with, to, or from persons located in California. You state that consumers purchasing goods and services using _____'s payment processing services "generally are not located in California." This implies that consumers *may* be located in California. You also state that _____ provides payment processing services *to* businesses located in California. This constitutes money transmission in California pursuant to Financial Code section 2003, subdivision (k).

³ Fin. Code, §2030, subd. (a).

B. FinCEN's Exemption for Payment Processors

You state that FinCEN exempts a payment processor from registering as a money services business ("MSB") if it meets four conditions. You state that _____'s payment processing activities for _____ and _____ cards satisfy all four conditions while its payment processing activities for _____ cards satisfy three out of four conditions. However, whether _____ satisfies the conditions necessary to exempt it from registering as an MSB with FinCEN is irrelevant to the determination of whether _____ is exempt from the MTA.

C. Agent of Payee Exemption

Financial Code section 2010, subdivision (l) exempts from the MTA transactions in which the recipient of the money is an agent of the payee pursuant to a preexisting written contract and delivery of the money to the agent satisfies the payor's obligation to the payee for the goods or services provided. "Agent" is defined as one who represents another, called the principal, in dealings with third persons.⁴ "Payee" means the provider of goods or services, who is owed payment of money from the payor for the goods or services.⁵ "Payee" means the recipient of goods or services, who owes payment of money to the payee for the goods or services.⁶

You argue that _____ satisfies the agent of the payee exemption because it receives funds from a consumer/payor and delivers the funds to a merchant/payee pursuant to a preexisting written contract. You state that under the Merchant Services Agreement ("MSA") entered into with each merchant, as soon as a payment transaction is authorized by a card company, the merchant's right to receive payment from the consumer purchasing the goods or services is replaced by the merchant's right to receive payment from _____. However, the MSA does not contain the language necessary to support your assertion. The MSA does not state that a merchant appoints _____ as its agent to accept payment from consumers on the merchant's behalf, for goods or services offered by the merchant. Nor does the MSA state that payments made by a consumer to _____ satisfy the consumer's obligation to the merchant.

You point to the definition of "transaction" in the MSA and argue that if a merchant accepts an approved card from a consumer, the consumer has no further payment obligation to the merchant. But the MSA does not explicitly state that payment authorization from a card company to _____'s financial institution satisfies the consumer's

⁴ Fin. Code, § 2010, subd. (l)(1) and Civ. Code, § 2295.

⁵ Fin. Code, § 2010, subd. (l)(2).

⁶ Fin. Code, § 2010, subd. (l)(3).

obligation to the merchant. Without explicit language in the MSA stating that _____ is the agent of the payee and that delivery of funds to the agent satisfies the payor's obligation to the payee, the requirements of Section 2010, subdivision (l) are not satisfied.

D. Factoring

You also argue that _____ does not require a money transmitter license because its activities represent factoring transactions rather than receiving money for transmission. You state that _____ is a "commercial factor" defined as a finance company that purchases a business's accounts receivable. As a factoring company, you state that _____ acquires from California businesses, a consumer's obligation to pay the business for goods or services rendered. You state that _____ acquires the obligation upon receiving a card company's authorization of the transaction, which occurs before money is paid by the consumer.

However, the MSA does not contain the language necessary to support your assertion. The MSA does not state that the merchant agrees to sell to _____ the account receivable generated by a consumer's obligation to pay the merchant for goods or services rendered, upon authorization of a transaction by a card company. Nor does the MSA state that a merchant releases its right, title, and interest to an account receivable upon sale of the account receivable to _____.

You point to _____'s designation as an "Acquirer" in the MSA and reference the definition of "account" under the California Commercial Code. You also state that _____ can charge back the merchant in the case of fraud or "a setoff or counterclaim" of a consumer against a merchant, to show that _____ is exposed to the credit risk of the sellers of accounts receivable like other factoring companies. However, these points do not establish that _____ purchases from merchants, accounts receivable generated by a consumer's obligation to pay the merchant for goods or services rendered, or that merchants agree to sell their accounts receivables to _____ upon a card company's authorization of a transaction. Because the MSA lacks explicit language reflecting a factoring arrangement between merchants and _____, _____ has not established that its activities represent factoring transactions rather than receiving money for transmission.

E. Public Interest Exemption

Financial Code section 2011 authorizes the Commissioner to exempt from the MTA any person or transaction if the Commissioner finds such action to be in the public interest and

the regulation of such person or transaction is not necessary. To make this determination, the Commissioner may consider various factors, including whether the person is licensed by a government agency and the risk and potential harm to persons located in California.⁷

You state that _____ does not transact business with California consumers and therefore, requiring _____ to obtain a money transmitter license would not further the consumer protection purpose of the MTA. However, as discussed in Section A above, you state that consumers purchasing goods and services using _____'s payment processing services "generally are not located in California" which implies that consumers *may* be located in California. You also state that _____ provides payment processing services *to* businesses located in California. Therefore, we disagree that California consumers and businesses are not at risk.

Because _____ has not established that it should be exempt from the MTA in the public interest or that regulation of its activities is not necessary, we disagree that _____ should be exempt from the MTA under Financial Code section 2011.

If you have any questions, please feel free to contact me at _____.

Sincerely,

Jan Lynn Owen
Commissioner
Department of Business Oversight

By
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Counsel

⁷ Cal. Code Regs., tit. 10, § 80.3002, subd. (b).