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By E-mail

Jennifer Rumberger
Senior Counsel
California Department of Business Oversight
Legal Division
1515 K Street, Suite 200
Sacramento, California 958144052

Re: Invitation for Comments on Proposed Rulemaking Money Transmitter Act: Agent of the Payee (PRO 7/17)

Dear Ms. Rumberger:

We are writing on behalf of Tipalti, Inc. ("Tipalti"), which welcomes the opportunity to submit its comments to the Department of Business Oversight (the "Department") regarding the proposed rulemaking to clarify the applicability of Cal. Fin. Code §2010(l).

Tipalti offers a software platform that allows businesses to consolidate and manage their accounts payable functions, and facilitates business-to-business payments made between companies and their suppliers of various goods and services. Tipalti provides these services to businesses across the world, including in California. In many cases, Tipalti may act on behalf of the payee in such transactions. Accordingly, Tipalti appreciates the Department's efforts to bring clarity to the circumstances under which such activities are exempt from the California Money Transmission Act (the "MTA").

These initial comments are provided on the topics highlighted by the Department in its invitation for comments in order to suggest some principles and policy implications for the Department's consideration at this early stage. Tipalti looks forward to an opportunity to continue its dialogue with the Department regarding the agent of the payee exemption as the rulemaking process moves forward, and to respond to specific regulatory language proposed by the Department once available.

A. Statutory Interpretation, Legislative Intent and Online Marketplace Platforms

The Department's invitation for comment indicates that, based on the legislative history of Assembly Bill 2209, which codified the agent of the payee exemption at Cal. Fin. Code §2010(l), the legislature, at minimum, wished to ensure that online marketplace transactions not be regulated as money transmission under the MTA. As it appears that online marketplaces and

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e-commerce transactions were at the forefront of at least some legislators' minds, including the bill's sponsor Assembly Member Dickinson, the Department is correct that any implementing regulations should not disrupt application of Cal. Fin. Code §2010(l) to online marketplaces and other e-commerce transactions. As reflected in our comments below, online marketplace platforms represent an evolving and dynamic part of commercial exchanges, and the existing and potential future functionality of these platforms should be taken into account in order to ensure that any regulatory language implementing the agent of payee exemption does not hamper the continued growth of one of the most dynamic sectors of the economy.

Notwithstanding the foregoing, we note that the legislature did not elect to include language in Cal. Fin. Code §2010(l) to limit its application to online marketplace platforms, or to e-commerce in general.[1] The plain language of the statute clearly and expressly sweeps much more broadly to cover handling of funds as agent of a payee in all transactions for goods or services, regardless of whether those payments originated in a physical or virtual environment. It is a fundamental tenet of statutory construction that resort to legislative history is inappropriate unless the language of the statute itself is ambiguous, which is not the case here.[2]

Furthermore, where the statutory language itself is unclear, before resorting to legislative history, a court must first consider the textual context.[3] In this case, in addition to codifying an

[1] We note that the brief bill summary used the Senate Banking and Financial Institutions Committee report, in the Senate Rules Committee report, and the Department of Finance Bill Analysis report indicate the bill would "ensure that electronic commerce (e-commerce) transactions are not inadvertently regulated as money transmission...". "E-commerce" is defined in AB 2209 to include "any transaction where the payment for goods or services is initiated via the Internet or a mobile device", and therefore extends more broadly than only those transactions initiated through marketplace platforms. Sen. Noreen Evans, S. Banking & Fin. Inst. Comm., 2013-2014 Sess., AB 2209 (Dickenson), at Summary (Cal. 2014); S. Rules Comm., 2013-2014 Sess., Third Reading, AB 2209, at Digest (Cal. 2014); Dep't of Fin. B. Analysis, AB 2209, at Bill Summary (Cal. Aug. 4, 2014).

[2] *See* Halbert's Lumber, Inc. v. Lucky Stores, Inc., 8 Cal.Rptr.2d 298, 303 (Cal. Ct. App. 1992)(providing that in reviewing a statute the words should be given their ordinary, everyday meaning and that if the meaning is not ambiguous, the language controls); Perrin v. U.S., 444 U.S. 37 (1979) ("A fundamental canon of statutory construction is that, unless otherwise defined, words will be interpreted as taking their ordinary, contemporary , common meaning."); U.S. v. Shreveport Grain & Elevator Co., 287 U.S. 77, 83 (1932), quoting Hamilton v. Rathbone, 175 U.S. 414, 421 (1899)(providing that legislative history should be "given consideration in determining the meaning of a statute, but only where that meaning is doubtful. They cannot be resorted to for the purpose of construing a statute contrary to its plain terms .... Like other extrinsic aids to construction, their use is to solve but not to create an ambiguity ").

[3] *See* Fluor Corp. v Superior Court, 354 P.3d 302, 316 (Cal. 2015) quoting People v. Cornett 274 P. 3d 456 (Cal. 2012)("We begin with the plain language of the statute, affording the words of the provision their ordinary and usual meaning and viewing them in their statutory context, because the language employed in the Legislature's enactment generally is the most reliable indicator of legislative intent. The plain meaning controls if there is no ambiguity in the statutory language.") (Emphasis added).

agent of the payee exemption, Assembly Bill 2209 added the definition of "e-commerce" to the MTA, and used the term in certain new substantive changes to the MTA. Notably, the legislature did not use that term in the agent of the payee exemption. If the legislative intent had been to limit the agent of the payee exemption to e-commerce transactions, the legislators certainly had the opportunity to use the same newly defined term as a limitation in Section 2010(l). Instead, they elected not to do so, confirming that Section 2010(l) must be read as written, i.e., as a broad exemption for entities that handle payments for payees, regardless of how those payments originated.

Accordingly, while the expressed priorities of the bill's sponsor and certain of its supporters indicate that the Department should take special care not to interpret that MTA in a way that would interfere with the application of the exemption to online marketplace transactions and e-commerce, the references to marketplace transactions and e-commerce do not provide a basis to interpret the statute in a manner that restricts its application to *only* online marketplace transactions and e-commerce, in substitution for the broader text adopted by the legislature.[4]

B. Definition of Goods and Services

Financial Code section 2010, subdivision (l) makes the agent of the payee exemption available in connection with the provision and receipt of good and services. The Department seeks comment as to whether "good and services" should be further defined and what appropriate limitations may exist to these terms. Given the broad ordinary meaning of "goods and services" and the ever-expanding scope of assets, rights, interests and benefits available on e-commerce platforms, the Department should maintain a broad interpretation of "good and services" to encompass assets, rights, interests and benefits of any kind or nature.

The legislature elected not to define "goods and services," and application of its ordinary meaning would include a wide, potentially universal, variety of commercial transactions. Such a broad understanding is consistent with the legislature's intent to not impede a growing and diversifying marketplace and ensure the MTA "does not create unnecessary barriers to entry for new entities wishing to enter the payments space."[5] In the past two decades, online marketplaces have exploded in size and scope, and even in the few years since the legislature passed Assembly Bill 2209, the scope of "good and services" available on online marketplaces has grown and shifted in unexpected ways. Online marketplaces offer all manner of tangible property for both

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[4] *See* N.L.R.B. v. SW General, Inc., 137 S.Ct. 929, 942 (2017)("What Congress ultimately agrees on is the text that it enacts, not the preferences expressed by certain legislators."); Oncale v. Sundowner Offshort Services, Inc. 523 U.S. 75, 79 (1998)("[I]t is ultimately the provisions of our laws rather than the principal concerns of our legislators by which we are governed.")

[5] Assemb. Roger Dickenson, Assemb. Comm. Banking & Fin., 2013-2014 Sess., AB 2209, at Comments (Cal. 2014) (indicating the purposes of AB 2209 are a continuation of those supporting AB 786 (passed Oct. 4, 2013)).

personal and commercial purposes, ranging from electronics, to perishable groceries, to industrial equipment. Non-tangible goods are also widely available for purchase and lease including music, movies and computer software. Housing rentals, transportation services by car, limo and helicopter, and an ever-expanding number of services including in-home furniture assembly, courier service, line waiting, translation services, and website building are also available through e-commerce. Each new expansion comes with the opportunity for new entrants, greater competition and transparency, and more consumer choice.

Given the unbounded expansion of e-commerce in recent memory and the likelihood of continued growth in the future, the Department should define "goods and services" broadly to encompass all commercial exchange of assets, rights, benefits and interests for consideration. A more narrow definition would have the result of arbitrarily favoring certain types of existing platforms or creating arbitrary barriers to entry for e-commerce providers that intend to expand to new areas. Indeed, in light of the existing scope of online marketplace and e-commerce activity, the choice between a broad definition of "goods or services" and those that are "typically available" on online marketplaces is a false dichotomy; many if not all of the examples of a "broad" definition are already supported in some fashion on online marketplaces: residential housing (Airbnb, HomeAway), real estate (Trulia, Hubzu), various forms of intellectual property (Amazon, iTunes, Shutterstock, eBay, Getty, Capterra, Google Play), and insurance (insurance.com, The Zebra).

Furthermore, drawing fine lines among various types of goods and service would create substantial practical difficulties. Third-party payment processors that facilitate payment for a variety of "goods and services" generally do not police the details of the goods and service handled in each transaction. Instead, processors rely on merchant representations that transactions are lawful and do not violate certain basic standards. While those representations may be supplemented by further diligence in certain circumstances, a new mandate to further categorize different types of transactions as falling within or without the broad terms "goods or services" would impose unnecessary burdens and costs on all market participants. If sufficiently challenging, such a mandate could have the result of overwhelming the benefit the legislature intended to convey in enacting this exemption.

C. Defining the "Receipt" of Goods and Services

Financial Code §2010(l) provides that for purposes of the agent of the payee exemption, the delivery of money or monetary value to an agent must satisfy the payor's obligation to the payee, and defines the payor as the "recipient" of the goods or services. The Department has asked whether the definition of "recipient" should be limited to persons that intend to consume, use or experience the good or service, in effect limiting the definition of "payors" to end users. The question indicates an overly narrow interpretation of the exemption, as well as an arbitrary preference for certain business models over others.

There are two considerations that guide our comments on the definition of "recipient." First, we are not aware of any basis for a narrow definition of the term "recipient" that would cover only persons (including entities) that physically receive or consume a good. Individuals or entities that receive goods, physically or constructively, with the intent to resell those goods are no less "receivers" of the goods under any ordinary meaning of the term. Indeed, consistent with the principles of statutory construction cited above, in the absence of a specified meaning, the term "recipient" must be read in accordance with its ordinary meaning. The Merriam-Webster Dictionary defines "recipient" merely as "one the receives" and "receive" as "to come into possession of." Black's Law Dictionary similarly defines "receive" as "to take" or "to come into possession of or get from some outside source." Nothing in the statute supports undercutting that ordinary meaning by reading into the statute language that does not appear, i.e., that a payor is a recipient of goods or services "solely for the purpose of consuming, using or experiencing those goods or services."

Furthermore, interpreting payor to exclude entities that receive goods or services for purposes of resale would result in the Department providing a preference solely for direct sale business models, in contrast to the broader language of the statute. As previously noted, while certain legislators and supporters of the Assembly Bill 2209 appeared to have online marketplaces as their focus, the agent of the payee exemption provides no indication in its text that it was meant to be limited to only marketplace transactions. If a business were to purchase goods and services either for its own use and for its inventory, and make a payment to a vendor through the vendor's contracted agent, there is nothing within the text of the exemption to indicate that such a payment should not fall within this exemption, or that goods purchased for the business' own use versus inventory goods should be treated differently.

Any difference in treatment between goods for corporate use and inventory goods is also likely to be burdensome for payment processing as it would require participants to segregate different transactions for different payment processor treatment without a compelling policy justification. For example, would a hotel purchasing bedding for in-room use be required to place a separate order for bedding sold in a gift store? Would a technology store be required to place separate orders for iPads used as mobile checkout systems from iPads resold to customers? Even asking these questions highlights the fact that such distinctions were not intended, are impractical and serve no policy purpose. Indeed, the statute does not indicate any intent to grant a preference to online marketplaces that do not take ownership of goods over other retail models that require at least temporary delivery of goods to the retail intermediary. To the contrary, the agent of the payee exemption is focused on risk to the payee that sold those goods; as long as payment to the intermediary constitutes payment to the payee, the use to which the payor then puts the goods received is irrelevant to the payee, as it is irrelevant to the purposes of the exemption.

Second, it would be inappropriate to read the definition of "payor" to impose a barrier to the application of the exemption when more than one intermediary, each acting for the payee, facilitates the delivery of funds to the ultimate provider of goods or services. Indeed, a typical online marketplace payment might take the form an end user (payor) making payment to the marketplace acting as agent of the ultimate seller (payee), and the marketplace in turn providing those funds to another agent of the seller (payee) to complete the delivery of payment. Provided the person that initiated the payment is protected (in that their obligation to pay has been satisfied), the Department should look at the transaction as a whole in applying an agent of the payee exemption, rather than focus on a limited definition of "payor" that could result in only applying the exemption to an agent that receives funds directly from the end user or only to the agent that is the last step in the delivery to the payee.

As previously noted, the legislature intended, at a minimum, that the MTA should not be applied in a manner that would burden online marketplaces that facilitate small businesses providing their goods and services to consumers at more competitive pricing. Much of the supporting testimony reflected in the legislative history was based on the premise that costs associated with money transmission licensure would ultimately fall on the small businesses that would "be forced to pay more to bring their products and services to market, thus harming themselves and consumers" or threaten the economic viability of certain platforms, preventing these business from being able to easily reach consumers at all.[6]

An interpretation of the MTA that would provide for an exemption only if a singular entity sits between the provider of the goods or services and the end user is inconsistent with the reality of e-commerce and payment processing. While certain money transmission may be facilitated by a singular agent who collects funds from the payor and directly provides those funds to the payee, that is not the reality of the online marketplace. The payment flow for online marketplaces does not generally look like this:

End User → Agent (Marketplace) → Merchant

But instead includes at least one, and often multiple, payment processors that assist in the facilitation of the payments, for example:

End User → Entity A (Marketplace) → Entity B (Processor) → Merchant

If the Department were to interpret §2010(l) in a manner that would not allow for multiple intermediaries, the result would be to eliminate the exemption for the very industry that the legislature sought to support.

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[6] Sen. Noreen Evans, S. Banking & Fin. Inst. Comm., 2013-2014 Sess., AB 2209 (Dickenson), at Summary of Arguments in Support (Cal. 2014).

For example, assume that an online marketplace is Entity A. The consumer makes a payment to Entity A and based on commercial agreements among Entity A, Entity B and the merchant/service provider, upon the funds reaching Entity A, the end user's obligation to make the payment is satisfied, and the merchant is obligated to provide the relevant good or service. Indeed, in many cases, the good or service would already have been delivered. For example, payment for a ride is not made until the ride is complete, so the rider/payor is never exposed to delivery of funds without delivery of services. Similarly, in the case of most business to business payments handled by Tipalti, payees are receiving payments in arrears for goods or services previously provided to the payor.

For reasons of specialization and scale, the marketplace platform, which receives payment in the first instance on behalf of the provider/payee, will generally rely on a payment processor, Entity B, also acting as an agent of the merchant/service provider, to pass the funds from the online platform to the merchant/service provider. In determining if the agent of the payee exemption applies to Entity B's activity, the Department should not ask whether Entity A "received" a service from the merchant and therefore qualifies as a "payor" merely because Entity B receives the funds directly from Entity A. Rather than transaction should be examined as a whole. An exemption that would have been available if the marketplace had elected to perform the payment activity itself should not automatically become unavailable because it is more efficient and cost effective for the marketplace to deliver funds to a payment processor acting for the merchant, as long as both Entity A and Entity B satisfy the requirements necessary to be an agent.

In this regard, we note that the Department previously has expressed the view that the payor's obligation to pay can only be extinguished once, and that if the payor's obligation to the payee is satisfied with the receipt of payment by the first party in a chain (Entity A in the above example), it could not also be satisfied by the receipt of payment by the second party in the chain (making Entity B in the example above ineligible to be an agent of the payee). This is an overly narrow reading of the statute, which provides "delivery of the money or other monetary value to the agent satisfies the payor's obligation to the payee." The focus of this language clearly is on whether the payor is exposed to payment risk by having delivered funds to the payee's agent. As long as the payor does not have such risk, the intent of the statute as a whole, and the exemption in particular, is satisfied.

Furthermore, as long as both Entity A and Entity B have agreed with the payee to act as the payee's agent for payment and have agreed that receipt of funds by Entity A or Entity B satisfies the payor's obligation to the payee, the language of the statute is literally satisfied as well. There can be no dispute that payment to Entity A "satisfies the payor's obligation to the payee"; the only question is whether the subsequent transfer to Entity B meets that standard. However, if Entity B and the payee have agreed, for example, that "receipt of payment by Entity B as your agent constitutes receipt of the payment by you and satisfies the payor's obligation to

you," the standard set by the MTA has been met. While it would be true that the payor's obligation had already been satisfied when funds were delivered to Entity A, it is also true that the payor's obligation remained satisfied when funds were delivered to Entity B. Since the legislative objective was to protect the payor against payment risk, it would be contrary to legislative intent to take the position that payment "satisfaction" can only be a momentary event rather than a status that continues from the time funds are received by Entity A, through delivery to Entity B and ultimately to the payee.

Accordingly, rather than requiring the Department and participants to examine each individual leg of a transaction to determine if the "payor" in such leg "receives" a good or service, we respectfully suggest looking to the transaction as a whole, and determining whether (i) the entity receiving funds is acting as an agent to the provider of the good or the service and (ii) whether the obligation of the person from which the payment for the good or service originated has been satisfied prior to or cotemporaneous with the receipt of money by that agent. By examining the transaction as a whole, the Department can review the true nature of the complete transaction, rather than look at the individual components of transaction that could not reasonably exist outside of the transaction as a whole.

D. Additional Agent-of-Payee Exemption

The Department's invitation for comment provided that if the Commissioner interprets Financial Code Section 2010(l) as only properly applying to a "simple, three-party online marketplace transaction," the Commission may be open to exempting a broader range of commercial transactions pursuant to its authority under Financial Code Section 2011. Such a narrow interpretation of Fin. Code §2010(l) is inconsistent with the text of the statute, and not justified by the legislative history. However, if the Department determines to apply such an interpretation, the Commissioner should provide an additional agency based exemption applicable to the broader range of activities identified above for the same policy reasons that apply to online marketplace transactions. Processors acting on behalf of payees do not create exposure to payors for loss or misdirection of funds since payment to the processor/agent is the equivalent of paying the payee itself.

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Tipalti appreciates the opportunity to provide comments on the proposed rulemaking regarding Cal. Fin. Code §2010(l). If you have any questions regarding our comments, please do not hesitate to call me at (202) 736-8683 or dteitelbaum@sidley.com.

Very truly yours,

David E. Teitelbaum

cc: Lisa Schlesinger, General Counsel, Tipalti