

April 20, 2020

Writer's Direct Contact
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BLui@mofocom***Via email to regulations@dbo.ca.gov***Department of Business Oversight
Attn: Pamela Hernandez
One Sansome Street, Suite 600
San Francisco, CA 94104***Re: PRO 07/17 – Money Transmission Act – Agent of Payee Exemption***

Dear Ms. Hernandez:

These comments are submitted on behalf of The Money Services Round Table (“TMSRT”) in response to the notice of rulemaking action (the “Draft Rulemaking”) relating to the implementation of the agent of a payee exemption under the California Money Transmitter Act, Cal. Fin. Code § 2000 *et. seq.* (the “Act”).

TMSRT Background

TMSRT was founded in 1988 as an information sharing and advocacy group for the nation’s leading non-bank money transmitters. Its current members are RIA Financial Services, Sigie Corporation, American Express Travel Related Services Company, Inc., Moneydart Global Services, Inc. and Travelex Currency Services Inc., Viamerica Corporation, Western Union Financial Services, Inc., and MoneyGram Payment Systems, Inc. These companies offer services including bill payments and funds transfers (domestic and international) through retail points of sale, the Internet, and mobile devices, as well as the sale of money orders and other payment instruments, and the issuance, sale, and reloading of stored value products. TMSRT members are licensed in all U.S. states that have nonbank licensing laws currently in effect, including in California, and are Money Services Businesses (“MSBs”) as defined by the Bank Secrecy Act (the “BSA”).¹

A payments services business is a business that is based on trust. Individual consumers and businesses obtain payments services (including funds transfers as well as other products and services that expand beyond the core remittance model) from non-bank companies that they believe are safe and sound, and they rely on these companies to, among other things, appropriately and timely deliver or otherwise make available their funds to businesses they

¹ 31 USC § 5311 *et seq.* and its implementing regulations at 31 C.F.R. Chapter X.

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patronize in order to pay for goods and services. A money transmission regulatory system that facilitates these services while also providing appropriate protections to the public engaged in such transactions provides enhanced public confidence in the industry. This, in turn, encourages consumers to utilize the offerings of the payment services industry. Thus, TMSRT supports the implementation and maintenance of fair, reasonable and consistent money transmission laws designed to protect consumers and the financial system. Our comments on the Draft Rulemaking are focused on advancing those goals.

General Comments on Draft Rulemaking

The Act provides that a “person shall not engage in the business of money transmission in [California] . . . unless the person is licensed or exempt from licensure under [the Act] or is an agent of a person licensed or exempt from licensure under [the Act].”² The Act exempts, however, a “transaction in which the recipient of the money or other monetary value is an agent of the payee pursuant to a preexisting written contract and delivery of the money or other monetary value to the agent satisfies the payor’s obligation to the payee” (the “Agent of a Payee Exemption”).³ With respect to the Agent of a Payee Exemption:

- “An agent is one who represents another, called the principal, in dealings with third persons,” as defined by Cal. Civ. Code § 2295.
- A “payee” is the “provider of goods or services, who is owed payment of money or other monetary value from the payor for the goods or services.”
- The “payor” is the “recipient of goods or services, who owes payment of money or monetary value to the payee for the goods or services.”⁴

The Department of Business Oversight (the “Department”) states in the Initial Statement of Reasons (the “Statement of Reasons”) accompanying the Draft Rulemaking that the Agent of a Payee Exemption “was meant to keep pace with the rapidly evolving payments and e-commerce landscape by exempting transactions where certain contractual requirements are met, and consumers and other payors are protected from having to pay more than once to satisfy their obligations.” Put differently, the primary basis for regulation under the Act—the need to protect a sender of funds—is lacking if the sender is at not risk of its payment obligation not being met as a result of the nonperformance of an intermediary.

TMSRT agrees that *if* a consumer is not placed at any risk of loss by making a payment for goods or service that is received by an agent of a payee as opposed to the payee directly the

² Cal. Fin. Code § 2030(a).

³ *Id.* at § 2010(l).

⁴ *Id.*

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payment transaction should not constitute money transmission under the Act. It is clear that this is the case where: (1) the payor has already received or contemporaneously receives the goods or services at issue; and (2) the payment to the agent of the payee extinguishes the payor's payment obligation *to the provider of the goods or services* at the time of payment.

Nevertheless, the purpose of the Act—the purpose of regulating money transmission activity—is broader than protecting consumers and also includes “maintain[ing] public confidence in financial institutions doing business in [California]” and “preserv[ing] the health, safety, and general welfare of the people of [California].”⁵ Given that the Agent of a Payee Exemption is self-executing and the Department does not require that a person relying on the exemption obtain confirmation of its applicability, it is essential that the obligations and liabilities of each intermediary facilitating an exempt transaction between a payor and a payee are clearly established.⁶ There is always the risk that companies will try to exploit any ambiguity in the exemption, which may, in turn, create risk for consumers and other participants in the e-commerce economy. Therefore, as reflected in our comments below, we believe greater clarity is necessary with respect to: (1) what constitutes a multiparty transaction that qualifies as a single, exempt, agent of a payee transaction under the Agent of a Payee Exemption; and (2) what contractual or other requirements must be met by each party to the transaction seeking to rely on the Agent of a Payee Exemption (whether as the exempt statutory agent or as an exempt common law agent).

If the obligations of each paying party in the chain of a transaction—starting with the paying consumer—are not clearly structured, participants in exempt agent of a payee transactions (including the providers of goods or services) may not understand the liability they are taking on, and consumers may be at risk in the event of an intermediary's nonperformance. Maintaining the integrity of the financial system and ensuring consumers are protected thus requires clear guidance from the Department on the regulatory expectations for non-regulated transactions. Greater precision regarding how agent of a payee transactions must be structured to fall outside the scope of the Act will help ensure that the delivery of funds from the consumer to the person providing goods or services to the consumer (*i.e.*, the payee): (1) does not involve unregulated money transmission creating risk of loss for an intermediary payor; and (2) does not result in loss or risk of loss to the consumer if the payee is unwilling or unable to deliver the consumer's goods and services either because the payee

⁵ Cal. Fin. Code § 2001(d).

⁶ The Statement of Reasons confirms that “[t]he agent of payee exemption is self-executing, meaning that an entity does not need the Department's prior authorization to rely on the exemption.” By contrast, other state banking departments—including in Kansas and Michigan—have determined that persons must request confirmation from the department that proposed or ongoing activities come within the scope of the exemption and are not subject to licensing. See https://www.michigan.gov/documents/difs/Agent_of_a_Payee_Procedures_659197_7.pdf (Michigan), and https://www.osbckansas.org/mt/guidance/mt2016_01_agent_of_the_payee.pdf and https://www.osbckansas.org/mt/agent_of_the_payee_instructions.html (Kansas).

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lacks the funds to perform its obligation or is not appropriately bound by the applicable agreement to deem the consumer's payment received upon receipt by the payee's agent.⁷

In short, TMSRT believes that caution is warranted with respect to a broad interpretation of the scope of exempt payee agent transactions. If the Department does not intend to provide companies with express authorizations or confirmations prior to engaging in activity under the Agent of a Payee Exemption, it is particularly important that any final rule, and accompanying final statement of reasons, precisely set forth specified criteria to come within the Agent of a Payee Exemption, and explain the basis for distinctions between regulated and non-money transmission activity under the Act. TMSRT is concerned ambiguity in the regulation could result in a lack of oversight of money transmission activity that puts payors and the financial system at risk. Consistent with this concern, our comments on the draft rulemaking address the following specific issues:

- The basis for certain limitations on the scope of the Agent of a Payee Exemption, as explained in the Statement of Reasons; and
- The concept of "successive agents" for a single transaction.

Comments on Specific Elements of the Draft Rulemaking

Limitations

Agent of a Payor or Sender. TMSRT agrees that an agent of a payor or sender cannot be eligible for the Agent of a Payee Exemption, and appreciates the Department's proposed affirmation of this point in § 80.126.10(b) of the Draft Rulemaking.

Stored Value. TMSRT also understands that the Draft Rulemaking would affirm that the Agent of a Payee Exemption "does not apply to the sale or issuance of stored value,"⁸ as defined in the Act. The Statement of Reasons explains, in part, that "[t]he payment obligation element cannot be met in the stored value context because no payment obligation exists, and no payee is identified." We are concerned that this statement conflates the nature

⁷ For example, if a consumer has purchased goods or services delivered or otherwise obtained at a future date, the consumer may still be at risk of harm if the payee lacks the funds to deliver the goods or services (or provide a refund) because the intermediary has not yet settled (or cannot settle) the funds to the payee. While not articulating this specific reasoning, the North Carolina Office of the Commissioner of Banks has concluded that the statutory agent of a payee exemption under the North Carolina Money Transmission Act, N.C. Gen. Stat. § 53-208.44(a)(8), does not apply to a payment for a future obligation because the payment obligation is not outstanding when payment is made, but rather when the transaction is consummated on a future date. *Declaratory Ruling 2017-01* (Jul. 10, 2017). Recent unexpected widespread cancellations of activities as a result of the COVID-19 pandemic highlight the potential differences in risk to consumers and to financial intermediaries between transactions involving a contemporaneous purchase of a good or service and transactions involving the payment for a good or service to be delivered or performed in the future.

⁸ § 80.126.20 of the Draft Rulemaking.

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of a regulated stored value product with a transaction involving the *purchase* of such a regulated stored value product. It is true that an issuer of stored value is holding funds on behalf of the holder of the stored value, and that the issuer has no specific, immediate obligation when receiving the funds to deliver the funds to another person. But stored value *is a payment obligation*.⁹

As such, we believe that the statement of reasons accompanying any final rule should clarify that a transaction involving the sale of a regulated stored value product¹⁰ is not exempt because it is a transaction involving the sale of a regulated money transmission product and therefore does not constitute the sale of goods or services “other than money transmission services.”¹¹ This distinction is important because in the context of a purchase or reloading of stored value, the issuer of the stored value *can be a payee*—even if the issuer cannot meet the definition of a “payee” under the Agent of a Payee Exemption—if the consumer is making a purchase of the stored value from the issuer, and the consumer’s funds are accepted by an intermediary as the agent of the issuer (or of a third-party distributor). In this case, however, the intermediary is an agent facilitating the sale or reloading of a regulated money transmission product, and therefore must be an authorized agent of a licensed money transmitter pursuant to Sections 2060 – 2063 of the Act.¹²

Charitable donations. The Draft Rulemaking would define “goods or services” as “any good or service, other than money transmission services, for which the payor has a payment obligation to the payee,” and would affirm that a “service” includes charitable purposes.¹³ The Statement of Reasons explains that the term “goods and service” is broadly construed and, therefore, the term “obligation” in the context of “goods and services” is also broadly construed. We interpret this provision to affirm that a charity can be a payee as defined by the Agent of a Payee Exemption. It follows that a payments services company that provides payment processing services to a charity as an agent of a payee and otherwise meets the criteria set forth in the Agent of a Payee Exemption is not required to be licensed in order to do so. We are concerned, however, that the Statement of Reasons also suggests that the requirements of the Agent of a Payee Exemption are not actually applicable to a payment processor for a charity:

. . . to the extent that a charity has appointed a person as its agent (under either general agency law or the agent of payee exemption) to accept funds on the charity’s behalf, the agent is

⁹ See, e.g., Cal. Fin. Code § 2003(r) (“‘Outstanding,’ with respect to . . . stored value, means issued or sold by the licensee in the United States and not yet paid or refunded by the licensee, or issued or sold on behalf of the licensee in the United States by its agent and reported as sold, but not yet paid or refunded by the licensee.”).

¹⁰ I.e., “stored value” as defined by Cal. Fin. Code § 2003(x).

¹¹ See § 80.126.30 of the Draft Rulemaking.

¹² See Cal. Fin. Code § 2030(a) (prohibiting a person in California from engaging in the business of money transmission unless, among other things, the person is “an agent of a person licensed” under the Act). This requirement would not apply to stored value that is exempt from regulation in California, however.

¹³ See § 80.126.30 of the Draft Rulemaking.

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considered not to have received money for transmission and therefore meets the spirit and purpose of the agent of payee exemption.

We respectfully believe that the statement of reasons accompanying any final rule should clarify that a payment processor acting on behalf of a charitable organization must meet the statutory requirements of the Agent of a Payee Exemption (as interpreted by the final rule). Otherwise, the statement of reasons should be very clear about why a payment processor for a charitable organization can be only a common law agent that meets the “spirit and purpose” of the Agent of a Payee Exemption, and why this flexibility would not apply to payment services providers for other types of payees. The suggestion in the Statement of Reasons that it should suffice to meet the “spirit and purpose” of the exemption calls into question the purpose of the statutory Agent of a Payee Exemption, and whether the Department believes that a person acting as an agent of a payee is a money transmitter *but for* the statutory Agent of a Payee Exemption.

Successive Agents for a Single Transaction

Section 80.126.10(a) appears to affirm that an agent of a payee, as defined by Cal. Fin. Code § 2010(l) (*i.e.*, the Agent of a Payee Exemption), “has not received money for transmission” and therefore is not engaged in money transmission under the Act. The Statement of Reasons indicates that § 80.126.10 “would clarify that there can be successive agents that facilitate the settlement of funds for payment,” and elaborates that:

Some of the agents may be common law agents and some may be statutorily defined agents of a payee. So long as one of the agents is an agent of a payee, such activity does not meet the definition of “money transmission.”

We respectfully believe that more clarity is needed regarding how the Department interprets the Agent of a Payee Exemption to apply to a transaction involving successive agents. By definition, we believe that the agent in direct contractual privity with the payee (*i.e.*, the actual provider of the goods or services purchased by the consumer) must be the entity exempted, by the Agent of a Payee Exemption, from regulation as a money transmitter.¹⁴ We also believe that only one entity per transaction can be exempt under the Agent of a Payee Exemption. The Statement of Reasons, which states that “the agent of payee exemption is only available one time per transaction,” indicates that the Department shares

¹⁴ This position is also consistent with the exemption under the BSA for a payment processor, which has been interpreted by the Financial Crimes Enforcement Network to *require* that the person claiming the exemption be in direct privity with the payee. *See, e.g.*, FIN-2013-R002, Whether a Company that Offers a Payment Mechanism Based on Payable-Through Drafts to its Commercial Customers is a Money Transmitter (Nov. 13, 2013) (affirming that that a payment processor’s agreement must be “with the seller or creditor that provided the goods or services and receives the funds from the” payment processor, and also that the agreement must “provide for the transmission of funds only to the creditor or seller with whom the payment processor is contracting and not to another location or person.”).

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this view. However, as noted above, the Statement of Reasons also suggests that, for a single transaction, “some” participants may be common law agents and “some” may be agents of a payee under the statutory definition. Given the importance of this rulemaking in guiding industry participants in determining whether they are engaged in regulated money transmission, we believe the language of the statement of reasons accompanying any final rule should be more precise.

Specifically, the statement of reasons accompanying any final rule should be consistent in affirming that there can be only one statutory agent of a payee, and that person must be in direct privity with the payee. Any other entity that either receives or transmits funds in connection with the consumer’s payment must be either a common law agent of the entity asserting the Agent of a Payee Exemption, or subject to regulation as a money transmitter. This construct is consistent with the *statutory* agent of a payee exemption, which establishes that the payment to the *statutory* agent of the payee extinguishes the payor’s obligation to the payee. That is, if payment to an intermediary is deemed payment to the payee—meaning that the obligation is extinguished under the statutory agent of a payee exemption—then there is no reason that intermediary cannot appoint its own agent, under the common law, to facilitate its acceptance of funds. However, as the Department has previously observed and as the Statement of Reasons and Draft Rulemaking affirm, there can be only one instance of a payment obligation between a payor and a payee per transaction.¹⁵ In turn, only payment to the payee can extinguish the payment obligation. Therefore, only the payee can appoint the agent whose receipt of funds extinguishes the payor’s obligation to the payee in accordance with the Agent of a Payee Exemption. That agent can appoint other common law agents to accept funds on *its* behalf by “stepping into its shoes,” but a common law agent cannot be a “payee” as defined by the Agent of a Payee Exemption because the common law agent is not the provider of the goods or services.

Consistent with this observation, we also believe that if a marketplace is a payee and the customer a payor, then for there to be a second transaction the marketplace must be the *payor* for that second transaction. We respectfully believe the Department should clarify how a marketplace can be a payor even if the marketplace does not “have title to, or possession of, a good or service provided to a consumer.” In this case, the marketplace would be an “indirect” *payee*, as defined by § 80.128 of the Draft Rulemaking. The Statement of Reasons appears to suggest that the marketplace could only subsequently be a *payor* if the marketplace, “as payor, purchas[es] goods from Merchant, as payee, to fulfill an order, or restock its own supply after a consumer purchase.” But the Statement of Reasons *also* suggests that both the marketplace and the merchant can each be payees even if the

¹⁵ See, e.g., California Department of Business Oversight, *Opinion Letter – Agent of Payee Exemption – Successive Agents* (Apr. 5, 2018) (observing that “The language of [the Agent of a Payee Exemption] requires that payment to an agent satisfy the payor’s obligation to the payee. The payor’s obligation cannot be extinguished twice.”). The Statement of Reasons affirms that “the agent of payee exemption is only available one time per transaction.”

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marketplace does not take title to the goods or services and is not paying the merchant to “restock its own supply,” as follows:

Customer -> Payment Processor 1 -> Marketplace -> Payment Processor 2 -> Merchant

Customer, as payor, purchases a good from Marketplace, as payee, and there is a payment obligation between Customer and Marketplace, constituting one transaction. If Merchant has appointed Payment Processor 2 as its agent by written contract (and other requirements are met), Payment Processor 2 would be eligible for the exemption.

The reference to “other requirements” being met would appear to suggest that there needs to be a *payor* (as defined by the Agent of a Payee Exemption) so that Payment Processor 2 can be the agent of the (merchant) payee consistent with the Agent of a Payee Exemption. We are concerned that industry participants will not be able to ascertain who the payor would be in such a situation, and therefore what types of transactions or aspects of transactions (*e.g.*, settlement to a third party merchant on behalf of a marketplace) would be subject to regulation as money transmission, if any. We believe this clarity is important and, therefore, the final statement of reasons should explain, on a step-by-step basis, how each participant in a multiparty transaction or series of transactions would or would not be subject to regulation as a money transmitter under the Act.

Conclusion

TMSRT believes that an effective money transmission licensing and oversight regime helps to maintain both consumer trust and the viability of payments services companies by ensuring that these businesses are operated on a sound financial basis and that consumer funds are not impaired. Any final Department rulemaking regarding the Agent of a Payee Exemption should therefore ensure that the scope of exempted transactions is clearly delineated so that all industry participants are able to understand the basis for the exclusion of applicable transactions.

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We thank you for your consideration of the items raised herein, and we would be happy to discuss them further at your convenience.

Sincerely,



Bradley S. Lui
Counsel to The Money Services Round Table