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Consultation on Payments System Modernisation (Licensing: Defining Payment Functions)

RESPONSE FROM STRIPE

19 July 2023

Overview

Stripe is writing in response to the request from the Australian Treasury for industry comments on the Consultation on Payments System Modernisation (Licensing: Defining Payment Functions) (“the Consultation Paper”). Stripe welcomes the opportunity to provide a submission to the Treasury as the Australian Government continues to make improvements to the regulatory framework for payments. In this submission, we provide an overview of Stripe’s business (see **Appendix A**) and feedback that addresses some of the key proposals outlined in the Consultation Paper for your consideration.

Stripe strongly supports the Treasury’s commitment to modernise the Australian payments system to ensure the regulatory framework is fit for purpose, and will provide the basis for another chapter of innovation and growth. It is widely recognised that, with the rapid acceleration in the internet economy and digital payments through the COVID-19 pandemic, the Australian payments landscape has become more complex and fragmented. That has created new challenges and opportunities for the government and regulators.

For Australia to seize the opportunity to further build its position as a leader in digital payments, the proposed regulatory framework should create a framework to guide the future development of the payments ecosystem in ways that drive growth, innovation, competition and security.

Stripe encourages the Government to take into account the following objectives as it develops a new licensing framework for payment service providers (PSPs) - so that any future regulation is fit for purpose and ensures:

1. **Australia is able to make the most of the opportunities presented by the online economy** - by pursuing measures that facilitate its growth and provide easy access to the internet economy for businesses and consumers.
2. **The foundations of the payments system remain strong** - by creating a level playing field for Payment Service Providers (PSPs) to maximise the benefits to innovation of diversity and competition within the ecosystem.
3. **Australia preserves and enhances its pro-innovation payments regulatory framework by retaining a distinctive regime for non-bank providers** that is proportionate and reflects their role, activities and risks.
4. **Strong domestic and international competitiveness** - by fostering and maintaining a regulatory regime that supports the development and deployment of new technologies, minimises the regulatory burden on PSPs and encourages market-based solutions in the payments sector.
5. **Recognition of the rapid evolution of the payments industry** and sufficient flexibility to be future proof and technology agnostic.
6. **Creation of the conditions for international connectivity** - by ensuring Australia contributes to the development of efficient, secure and accessible cross-border payments, and pursuing a domestic and international policy approach which supports strong connections and a high degree of interoperability with payments systems in other jurisdictions, including those in high growth Asia Pacific markets.

Executive Summary

Following is a summary of the key recommendations in Stripe's response:

- The addition of a **new principle** that the development of the new regime should seek to minimise the regulatory burden on businesses and ensure the costs of compliance are commensurate with the risk. Stripe is supportive of the Treasury's

proposal to identify opportunities to streamline the licensing and authorisation of PSPs.

- Consideration of **broader categories of payment functions** (which could be complemented by more granular guidance on the regulatory perimeter if needed) such that new products/innovations can easily fall within the broader categories rather than requiring a new or amended application as products are developed.
- Implementation of an **initial review period** to allow for updates to the framework, as well a reasonable grace period to allow sufficient time for compliance and regulatory measures to be implemented.
- In the context of standard stored-value facilities, providing a **definition of 'making payments' which should not capture business accounts** set up for acquiring services with the sole purpose of enabling the PSP's merchants to 'receive' payments for goods/services.
- Further clarity on what participants in the payment initiation services function would be captured by the definition, with a view to ensuring **only direct participants** are captured.
- Distinguishing between technical service providers and payment facilitators in the context of pass-through digital wallets, with a view to **excluding technical service providers from PFS regulation**.
- **Harmonising the AML framework with the payments licensing framework**, including leveraging or amending existing remittance service definitions in place of the proposed 'money transfer services' function to ensure consistency and avoid additional overlapping legislative concepts.
- Including merchant business accounts (as defined in this response) as a form of **limited purpose or limited participant facility**.
- **Narrowly defining 'consumer'** based on existing regulatory definitions, excluding small businesses in light of existing small business protections and to take into account that some consumer protections are not appropriate in a business context.

Stripe's response to the Consultation Paper

The feedback below is grouped according to key themes set out in the Consultation Paper, with cross-references to the Consultation Questions (CQ) that the feedback may be relevant to.

Part 2 - List of payment functions

Principles that should be considered (reference CQ1)

- We support the principles articulated by the Payment System Review to drive the development of a list of payment functions requiring regulation. We would, as noted above, underline the importance of ensuring the new licensing regime is developed in a way that ensures it remains fit for purpose as the sector continues to innovate new products, services and business models. We encourage the Treasury to take the time to thoroughly consider the changes, and industry views, and to avoid working towards strict timelines that could precipitate hasty decision making.
- Any new licensing regime should also be calibrated and applied in a way that allows for the supervision of entities according to the nature, method and volume of activity they are undertaking, thereby supporting the effective delivery of regulation and supervision commensurate with the specific risks posed by the activity.
- We would therefore suggest adding a principle that the development of any new regime should seek to **minimise the regulatory burden** on businesses and ensure the **costs of compliance are commensurate with risk**.
- Stripe is supportive of the Treasury's proposal to identify opportunities to streamline the licensing and authorisation of PSPs.

Future proofing the framework (reference CQ2, CQ7 and CQ8)

A holistic approach

- Stripe considers that a more holistic approach to a payment service provider's **(‘PSP’) products and services** should be taken into account when setting out the regulatory obligations that correspond to each payment function.
- In particular, if each payment function attracts different regulatory obligations, there is the potential for components of one funds flow (or one product, if it involves multiple payment functions) to be regulated differently - despite only one transaction taking place. This could result in different compliance measures required for different 'legs' of a transaction, while the product experience and corresponding controls cannot be easily separated in the same way.
 - For example, certain products provided by PSPs may involve the issuance of a payment account, payment initiation services and payment facilitation in the one. In this instance, it would be appropriate to consider the product as a whole as one payment function, and apply a uniform set of regulatory obligations, rather than treating each component of the funds flow/ product differently from a regulatory perspective.
- In order to allow for innovation and dynamic movement within the various payment functions rather than slowing down product development, it may be appropriate for the Treasury to consider **broader categories of payment functions** such that

new products can easily fall within the broader category rather than requiring a new application for an additional payment function. For example, the Treasury could consider just two payment functions (such as Stored-value facility ('SVF'), Payment facilitation services ('PFS')) and simply differentiate the regulatory obligations under the PFS function depending on whether the PFS is 'consumer' or not 'consumer' facing (see our comments in Part 7 below on the 'consumer' definition), which takes into account the level of risk posed by a PFS.

Review of payment functions (reference CQ7)

- In implementing Principle 2 set out in the Consultation Paper ('Ensuring the list can change and adapt'), **an initial review period** could be set to enable updates to the list following implementation of the framework. This will allow payment system participants to provide further feedback on what is working and what is not working from their perspective, and will ensure the regulatory framework is future proof and dynamic.
- Stripe also seeks Treasury's guidance on what **grace period** will be provided to payment system participants to ensure industry participants have sufficient time to assess the regulatory implications and put in place appropriate compliance and regulatory measures after the framework takes effect. Given the likely resource implications, we suggest a phased approach to implementation by providing an appropriate period (e.g. 1 year) from the time the relevant legislation and regulatory standards are issued .

Part 3 - Description of payment functions

Stored-value facilities: Issuance of payment accounts or facilities ('traditional SVFs')

- The definition proposed for this payment function specifies that the store of value is held *"for more than two business days"* and used *"for the purpose of making payments for goods and services or transferred to another person"*.
- It is not clear what 'making payments' is intended to capture. Stripe considers that 'making payments' should not capture business accounts (described below in more detail) that are set up as part of a PSP's merchant acquiring services, for the purpose of enabling the PSP's merchants to 'receive' payments. As such, it would be helpful to include a **definition of 'making payments'** in the framework and to differentiate this from these types of business accounts.

Business accounts should be excluded from SVF

- We submit that the definition of SVF **should not be overly broad and should not capture business accounts** that only enable businesses to record and *receive payments* for goods/services and do not enable users to make payments to third parties.
- As part of merchant acquiring services, some PSPs would provide their merchants with online accounts in which proceeds of transactions relating to purchases of goods and services are recorded (for example, these accounts may be provided to operators of online marketplaces and other platforms). We have outlined some of the key features of these accounts below:
 - *Information on sales transactions.* These accounts provide merchants with information on the sales and financial status of their business, and are intended to serve as an administrative record of funds. All of the funds recorded in these accounts relate to or originate from underlying goods and services transactions, and would be paid out to the merchants based on contractually agreed arrangements and timeframes. These accounts are not intended to store value or enable merchants to make payments to third parties.
 - *Apportionment between marketplaces and sellers.* In the case where acquiring services are provided to the operators of an online marketplace/platform, funds may initially be recorded in the platform or seller's account and may subsequently be apportioned between the platform and the sellers. The apportionment would be made in accordance with the agreements between the parties on the revenue share of a goods/services transaction made on the platform.
- Such merchant accounts, which are set up primarily for the purpose of recording and receiving funds for goods/services provided by the merchants, and apportionment of funds between an online marketplace/platform and its sellers, in connection with underlying goods/services transactions, should **not be considered as SVFs**. This is because:
 - **Accounts are not used to store value or pay third parties.** These merchant accounts are not intended to be used to store value or make payments to third parties. Rather, we want to confirm that the reference to 'making payments' in the definition of SVFs should refer to payments to third parties (ie. parties other than persons providing the goods or services which the funds relate to) rather than platforms paying out funds received from goods/services transactions to sellers, or merchants/sellers paying out funds to their designated bank accounts from an account set up by a PSP solely for

the purposes of providing acquiring services to the merchants (i.e. merchants *receiving* payments).

- **No additional risks.** There are no incremental risks posed by the functionalities offered by these merchant accounts, on top of the risks associated with merchant acquisition services, that should trigger additional regulatory requirements. As mentioned above, these merchant accounts are provided by PSPs as part of merchant acquiring services. The settlement of funds in the merchant accounts to the merchant, and the apportionment of amounts between the platform and sellers should not change the nature or the level of risk involved. This is because these transactions relate to the underlying goods/services transaction between the end customer/consumer and the platform/seller that was processed by the PSP. As noted in the Consultation Paper, merchant acquiring services will be regulated as a PFS under payment facilitation, authentication, authorisation and processing services. Risks arising from acquiring services should be adequately addressed by the regulatory framework and obligations relating to merchant acquiring services.
- We note that this approach is in line with the objectives set out in the CFR's report on the Regulation of Stored-value Facilities in Australia and the Treasury's Consultation Paper; namely, **to address the risks of third parties storing value on behalf of consumers.**
 - The CFR's recommendations and the proposed framework are intended to primarily address the risks relating to stored value facilities provided to consumers, where consumers top-up an e-wallet with their funds, which can then be used to make purchases for goods/services (as opposed to a merchant business account).

Payment facilitation services (reference CQ3, CQ7, CQ8, CQ9 and CQ23)

Payment initiation services

- The definition proposed for this payment function specifies that the payment instruction must be "*with respect to a payment account or facility held at another PSP*".
 - Stripe therefore considers that it is not the intention that this payment function captures accounts held by merchants with a PSP, and any instructions given by the merchant in respect of the movement of those funds held by the PSP (because the PSP is both the provider of the account and the party taking instructions in relation to that account).

- It is not clear what participants in the payment initiation services function would be captured by the definition. For example, in respect of an account to account payment system such as PayTo, Stripe considers that **only direct participants should meet the definition** as the initiator of a transaction. Having regard to CQ3, if this service is regulated as a “financial product”, it would also be helpful for the Treasury to clarify to what extent a person who facilitates these types of transactions (rather than a direct participant) could be considered to be “arranging” in relation to the service.

Payment facilitation, authentication, authorisation and processing services

- It is intended that this payment function captures PSPs such as pass-through digital wallets, defined as “*services that enable payment instructions to be transferred (facilitated)*”. As such, a digital wallet that does not store value but is linked to a debit card issued by a third-party may involve three types of payment functions: (i) the debit card as an issued payment instrument; (ii) the debit account that is linked to the debit card as an SVF function; and (iii) the digital wallet that *facilitates payments* on behalf of the customer as a payment facilitation function.
- Stripe notes that **a digital wallet of this kind may involve two distinct services**: one being the card ‘vault’ or back-end technical service provided to the consumer to enable them to link payment methods to the wallet (ie. *adding* an existing debit card to the wallet), and the other being the payment facilitation service (ie. *using* the debit card through the wallet to make a payment). We submit that the back-end technical service provider, which is not involved in the funds flow and does not handle funds, should not be regulated as a PFS based on the significantly lower level of risk - rather, it is Stripe’s view that only the payment facilitation service is and should be regulated as a payment function in the context of a pass-through digital wallet.
- In this context, Stripe notes that the Singapore framework excludes technical service providers (such as providers of data processing and storage services, data and entity authentication services) from regulation. The Treasury may want to consider a similar exemption.

Money transfer services

- In our feedback in Part 7 below, Stripe notes that further clarity and harmony between the proposed financial services regulation of payments and the anti-money laundering (‘**AML**’) laws would lead to a more transparent, holistic and effective regulatory framework. The introduction of a money transfer services category has

the potential to cause confusion if it is not clearly and thoughtfully **harmonised with the remittance service definitions under the AML laws**.

- The Consultation Paper states that the definition of ‘designated remittance arrangement’ (**‘DRA’**) under AML law is intended to be broader than the proposed ‘money transfer service’ definition. However, it is also intended that ‘money transfer service’ captures remittance service providers. It is therefore not clear:
 - in what instances a PSP would not be captured by ‘money transfer service’ if the PSP meets the DRA definition;
 - whether the intention is for money transfer services to be limited to pure remittance (such that there is no overlap with acquiring / payment facilitation services).

Part 4 - Excluded and exempted activities

Additional exclusions for consideration (reference CQ15)

Technical Service Provider

- As noted above at Part 3 with respect to Payment facilitation services, the Treasury may want to consider a similar exemption for technical service providers (such as providers of data processing and storage services, data and entity authentication services) as set out in the Singapore framework.

Part 7 - Overview of possible regulatory obligations

Consumer vs non-consumer facing (reference CQ20)

- The Consultation Paper proposes a different regulatory approach based on whether a PSP is ‘consumer facing’ or ‘non-consumer facing’. Stripe notes that the Consultation Paper also refers to ‘customer’ facing in certain instances, including in CQ20. Stripe submits that this distinction should be based on whether the PSP is ‘consumer’ facing rather than the broader reference to ‘customer’ facing.
- Stripe recommends that an existing regulatory definition be referred to in defining ‘consumer’ for this purpose so as to avoid multiple different definitions across regulatory frameworks. For example, a consumer may be defined as a person who purchases goods and services for personal, domestic or household use or consumption.
- Stripe further submits that **small businesses should not be included in the definition of ‘consumer’** for this purpose, for the following reasons:

- For PSPs that provide products and services to merchants exclusively for business-related purposes (such as the sale of goods and services) as opposed to personal, domestic or household use or consumption, the additional consumer regulatory obligations would not be proportionate to the risks posed.
- Contractual consumer protections already apply to small business customers in the form of unfair contract terms and consumer guarantees.
- Some consumer protections are not appropriate in a business context. For example:
 - Complaints made to AFCA by small business customers often relate to seeking redress for lost chargeback disputes - these disputes are decided by the card issuer and *not* the PSP such that the PSP is often not the appropriate party to the complaint and the compliance burden in responding to the complaints is material.
 - The requirements set out in the ePayments Code are drafted with a merchant's end-customer in mind and are not always easily applied in the context of a PSP providing services to a merchant for the purposes of enabling them to receive payments for goods/services. For example, the liability provisions apportion liability when a 'user' reports an unauthorised transaction on a card account. However a PSP is not the provider of the card account in this instance, nor is the 'user' (ie. the end consumer) the PSP's customer.
 - The hawking prohibition intends to protect consumers being approached with unwanted financial products through unsolicited contact. This is less relevant to PSPs whose customers are businesses and the PSPs are unlikely to offer their products during unsolicited contact.

Interaction with AML regulation (reference CO24)

- Stripe notes that there is a distinct absence of clarity in the Consultation Paper with respect to **how the new payments regulatory framework will interact with AML regulation**. Streamlining these two frameworks will be crucial in simplifying, harmonising and clarifying regulation applicable to the payments system, and would enhance the transparency of regulation in a more holistic manner. Unlike other jurisdictions such as the United Kingdom and Singapore, Australia's financial services regulatory framework is separate from the AML regulatory framework, such that this clarity will be crucial to achieving the Treasury's principle of improving regulatory certainty for PSPs.

Thank you once again for the opportunity to provide this submission. We would be happy to discuss these matters with you further.

Sincerely

Stripe Payments Australia Pty Ltd

Appendix A

About Stripe

Stripe is a global technology company that builds economic infrastructure for the internet. Businesses of every size - from startups to scaleups to public companies - use the company's software to accept online payments and simplify running an internet business.

Stripe partners with established financial institutions including banks, card schemes and payment methods. We are closely integrated with payment rails as a direct member of global card networks such as Visa, Mastercard and American Express, and through direct connections with national schemes such as eftpos in Australia. Stripe combines economic infrastructure with a set of applications for new business models like crowdfunding and marketplaces, fraud prevention, analytics, and more. Our tools help companies grow their business across borders.

Our founders - Irish entrepreneurs Patrick and John Collison - had experienced first-hand the difficulty of accepting online payments in an earlier business the two had launched together. On almost every front, it was becoming easier to build and launch an online business. Payments, however, remained dominated by clunky legacy providers. It seemed clear that there should be a developer-focused, instant-setup payment platform that would scale to support a business of any size. Stripe was formed to solve this problem and launched in 2011.

Only about three percent of GDP happens online today. Stripe wants to help more companies get started and thrive, and ultimately to grow the GDP of the internet. In addition, the Covid-19 pandemic has served to highlight the importance of having a resilient and innovative payments system, and we are providing the infrastructure to help Australian businesses to adapt and thrive.

We have been in Australia since 2014 and are growing rapidly. We have an Australian Financial Services License. We work with clients ranging from start-ups to ASX listed companies, including Catch, Canva, CultureAmp, ServiceM8, Atlassian, Xero and Covi. Globally, 43 percent of businesses who start on Stripe are run by first time entrepreneurs. However, one of the trends we have observed in Australia are traditional enterprises now leveraging Stripe the way digital natives have for years. The transformation is occurring across different sectors, including retail, insurance and education. 100,000 new businesses signed up to Stripe in Australia and New Zealand in 2021. Our survey research has shown that 70% of Stripe businesses in Australia double their monthly volume after two years.