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Department of the Senate
PO Box 6100
Parliament House
CANBERRA ACT 2600
By email: FinTech.sen@aph.gov.au

Dear Sir/Madam,

Consultation – Financial Technology and Regulatory Technology Inquiry

PayPal is grateful for the opportunity to lodge a submission to the Senate Select Committee on Financial Technology and Regulatory Technology (**the Committee**) regarding the inquiry into the current state of Australia's FinTech and RegTech industries (**the Inquiry**).

PayPal recognises the complex regulatory environment in the financial services sector and is pleased to provide specific comments in relation to the Committee's issues paper.

About PayPal

PayPal has been operating in Australia since 2005 and has more than 8 million active customer accounts. PayPal enables Australian businesses to transact online and offline, from sole proprietors and developers to established large merchants. The PayPal service is provided by PayPal Australia Pty Limited (ABN 93 111 195 389) which holds an Australian Financial Services Licence number 304962.

Through a combination of technological innovation and strategic partnerships, PayPal creates better ways to manage and move money, and offers choice and flexibility when sending payments, paying or getting paid. Available in more than 200 markets around the world, the PayPal global platform, including Braintree, Hyperwallet, PayPal Working Capital, PayPal Credit, and Xoom, enables consumers and merchants to receive money in more than 100 currencies, withdraw funds in 56 currencies and hold balances in their PayPal accounts in 25 currencies.

The Australian payments landscape is evolving at an unprecedented pace. As a global innovator in online payments, PayPal welcomes the opportunity to share insight and knowledge on both the opportunities and threats facing the payments

industry, and to encourage innovation alongside responsible management of growth and change.

As a facilitator of online commerce, PayPal enables transactions for Australian businesses, from sole proprietors to established large merchants, whilst protecting the personal financial information of its 8 million active user accounts. PayPal is passionate about innovation in payments and is excited about the myriad benefits that such innovation can bring to the Australian economy.

PayPal's digital wallet allows a user to have choice over how they want to pay. The choice of payment options afforded allows buyers to choose the manner in which they fund the payment, whilst not requiring them to disclose potentially sensitive financial information. PayPal thus offers buyers and sellers a better way to pay and get paid by providing:

- **Convenience.** Consumers only have to enter their payment and shipping details once into the PayPal system, reducing the need to duplicate data input for multiple merchants.
- **Privacy.** The merchant does not see the financial details of the consumer, because the information has already been stored in PayPal's record management system.
- **Assurance.** A secure, closed loop system, where PayPal can identify both sides of a payment, with in-built buyer and seller protection plans.
- **Real time payments.** The seller's PayPal account is credited, and buyer's account is debited in real time.
- **Fee transparency.** Merchant fees more accurately reflect the cost of processing the payments, and are not aimed at subsidising incentive payments to customers.
- **Risk management.** PayPal manages transaction risk for buyers and sellers which forms part of its cost base.

Below are our responses to the questions posed in the Inquiry:

1. What area of technological innovation does your company specialise in?

PayPal's service enables our customers to send and receive payments. We operate a two-sided network where both merchants and consumers have PayPal accounts with stored balance functionality. Since PayPal serves as a proprietary payment method that is accepted by merchants, we are more than a connection to third-party payment networks. Our service enables the completion of payments on our payments platform on behalf of our customers.

We offer our customers the flexibility to use their accounts to purchase and receive payment for goods and services, as well as to transfer and withdraw funds. We enable consumers to exchange funds more safely with merchants using a variety of funding sources, which may include a bank account, a PayPal account balance, a PayPal Credit account, a credit or debit card, or other stored value products such as coupons and gift cards. Our PayPal products also make it safer and simpler for friends and family to transfer funds to each other.

We offer merchants an end-to-end payments solution that provides authorisation and settlement capabilities, as well as instant access to funds. We help merchants connect with their customers and manage risk. We enable consumers to engage in cross-border shopping and merchants to extend their global reach while reducing the complexity and friction involved in enabling overseas and cross-border trade.

2. In general terms, how would you describe the operating environment for FinTech and RegTech start-ups in Australia?

Australia is a leading market internationally for FinTech and RegTech firms due to its open market economy and sound regulatory environment.

In Australia, we are licensed as an authorised deposit taking institution, but limited to providing purchased payment facility with the Australian Prudential Regulatory Authority (APRA). Purchased payment facilities are subject to minimum capital requirements, reviews of risk management process, and audits for a variety of practices. While this is less regulatory scrutiny than a bank would be subject to, it is a unique hybrid regime with appropriately strict requirements.

Fuelled by a fundamental belief that having access to financial services creates opportunity, PayPal is committed to democratising financial services and empowering people and businesses to join and thrive in the global economy. Our open digital payments platform gives PayPal's 295 million active account holders the confidence to connect and transact in new and powerful ways, whether they are online, on a mobile device, in an app, or in person.

3. What are the biggest opportunities and challenges for your business in the short-to-medium term?

The movement towards mobile payments is a major opportunity for our business. Consumers now expect context-driven experiences over intent-based experiences. Consumers are moving to mobile as their primary computing device, and as they do,

they expect seamless mobile commerce experiences at the point of discovery. With smaller screened-devices, and as commerce moves into new contexts like artificial and virtual realities or virtual voice assistants, where consumers no longer have good input devices, consumers expect that their mobile devices and apps know enough about them to eliminate the need for data entry.

Consumer and small business credit are another major opportunity for PayPal. We signed a long-term strategic partnership agreement with Citi Australia to further develop consumer credit products for PayPal's customers in Australia. Our PayPal Working Capital Lending has been a particularly exciting area for FinTech development. PayPal's research, conducted in 2019, found that 75 per cent of Australian businesses think the process of getting approved for finance is more difficult than it used to be, while 67 per cent think it's becoming a barrier to doing business.

PayPal's research found half of SMBs were more worried than they were last year about cash flow. Over a quarter (28 per cent) said they were always worried about cash flow. PayPal Working Capital launched in Australia less than five years ago, and with over \$AUD500 million now issued to more than 7,000 businesses, we can see that there is an ongoing demand for alternative finance solutions to support small businesses and to help them thrive. Information asymmetries were a tremendous challenge in traditional credit scoring. Most of the data involved in calculating a traditional credit score came from traditional financial institutions. Lower income, younger, and minority consumers and small businesses often lacked the prerequisite paper trail to document their historical payments and credit flows and therefore were considered risky lending propositions. Alternative data elements enable lenders to say 'yes' in cases where previously they would have been unable to do so.

The lack of a secure, reliable, digital identity framework poses a significant barrier to more efficient online interactions and economic participation by citizens least able to overcome those barriers. The fact that dozens of institutions are forced to repeat the same identity verification activities, for the same person, across multiple platforms to satisfy anti-money laundering, sanctions monitoring, and fraud risk management obligations is a material drain on economic resources. A 2017 Thomson Reuters study found that more than half of all banking salespeople are spending one-and-a-half days each week onboarding new client organizations.ⁱ Creating a secure government-issued digital identity framework linked to an electronic know your customer (e-KYC) could greatly improve the ecosystem for onboarding, authentication, and verification for electronic payments.

The Digital Transformation Agency's (DTA) efforts in this space are an exciting development. PayPal is encouraged by the DTA's progress to date and would welcome the opportunity to engage with the agency as the rollout of the *Digital Transformation Strategy 2018-2025* continues. Streamlining digital identification processes is vital to the long-term health and efficiency of the ecosystem.

Finally, risk and security are at the heart of everything we do at PayPal and is a major opportunity for us going forward. We strive to be a trusted player by our regulators as a company that embraces our regulatory responsibilities and always does what's right for our customers. These responsibilities include taking serious measures to combat money laundering and related financial crimes, which can be an issue in the small business financing space. We use data analytics, machine learning and visualisation to detect suspicious behaviour within 15 milliseconds and prevent cybercrimes. We process approximately more than 3.1 million transactions across the globe each day or USD20,705 payments each second, simultaneously giving users the promise of security where they 'shop' without sharing their data. Our most distinct value proposition is around leveraging data for risk mitigation. This is for reducing fraud and around reporting for money laundering, compliance, and sanctions perspectives.

4. What are your views on recent and forthcoming changes to policy settings and regulatory initiatives affecting the sector (e.g. implementation of the new Open Banking framework; introduction of the NPP in 2018; and ASIC's FinTech regulatory sandbox)?

PayPal Australia is generally supportive of an approach to Open Banking which provides customers with choice, convenience, and confidence. The framework represents a considered and reasonable approach to how Open Banking should be implemented and establishes a sound regulatory approach on which to base the broader Consumer Data Right. We are looking forward to July when access to data from the big four financial institutions will be more widely available, as well as to the continued rollout of the initiative. We hope that the regime leads to institutions creating free, open, and secure APIs that third parties can access to provide new financial services.

We believe one of the biggest opportunities around Open Banking is related to identity verification. PayPal strongly supports that banks as data holders will be obliged to share the outcome of identity verification assessments performed on a customer, provided the anti-money laundering laws are amended to allow data recipients to rely on that outcome. PayPal believes the sharing of data to confirm identity for the purposes of regulatory obligations should be permitted to be

securely and confidentially shared between institutions. This will limit customer inconvenience and improve efficiency of identification procedures for all financial service providers.

PayPal has been supportive of ASIC's review of the ePayments Code. We believe that the Code should be forward-thinking and competitively neutral. We have recommended to ASIC that proposal B5 on mistaken internet payments be simplified to help providers. We have also proposed that the Code be updated to account for NPP transactions and address the lack of a scalable dispute process in the event of fraud or mistaken payments.

Significant technological advancements have occurred since the last holistic review of the Code. PayPal would encourage a clear and concise Code that sufficiently accounts for market shifts. We have suggested that the requirements for terms and conditions be included in the scope of the review. Some of the requirements in the Code are inconsistent with regulations, including the *Corporations Act 2001*. Creating harmonisation on terms and conditions regulation can help providers with compliance and service provision.

We are supportive of the NPP. Faster access to payments is one of the largest demands we hear from our merchants and consumers. One item to consider as the NPP continues to develop is whether non-banks can participate in the scheme. India, for example, is currently considering allowing non-banks to access its core payments architecture. Innovative FinTechs could potentially leverage such access to provision new services.

Finally, ASIC's FinTech regulatory sandbox is a useful and highly adaptive innovation which is a benefit for early stage start-ups moving to commercialisation. The model provides a useful, but short period during which its compliance requirements will be limited and therefore less burdensome on a fledgling company. There is the potential that a start-up leveraging the sandbox to create a unique offering will become a potential partner for PayPal. The sandbox has benefits in continuing the development and growth of the FinTech ecosystem.

5. Do you have any suggestions on how the Australian Government can best facilitate the continuing growth of the FinTech and RegTech industries in Australia?

In the world of pervasive, rapid development of FinTech and RegTech, Australian regulators should focus on activity-based regulation, rather than entity-based regulation. This means that anyone providing a payment service is subjected to the

same regulatory regime, no matter what the entity is, or what the business model is. Activity-based regulation is business-model neutral.

Australia should also consider “risk-based” proportional authorisation, where the rules and regulations that apply to you should depend on the level of risk of your service. By creating a payment institution category, it has allowed entities that provide only payment services to do so in a regulated setting without needing to apply for a full and onerous banking license. The provision of payment services entails different kinds of risk than the provision of services a full bank does (credit, mortgages, lending etc.), and therefore the different legal requirements should be applied.

Finally, FinTech is a global phenomenon and requires collaboration between regulators across borders if it is to truly transform and democratise financial services. The FinTech bridge with the UK is an excellent first step and can be built upon. Creating interoperability through passporting regimes is the ideal method for enabling FinTech to develop. An example of a successful model comes from European Union where an entity regulated in a single market in the EU can passport their regulatory status into other countries that are part of the Union. This model would enable far more rapid scaling of innovative and beneficial financial services solutions.

6. To what extent should government encourage or incentivise the disruption of existing financial services business models by new market entrants, as opposed to promoting partnerships between new and incumbent players? Are these aims mutually exclusive?

At PayPal, we believe that FinTech is not about disruption; it is about value creation through enablement – the creation of value for everyone in the expanding digital economy, by enabling consumers, merchants, traditional financial leaders and technology leaders to participate in the global movement to the digital mobile economy.

We have learned that FinTech can be an enabler of the entire ecosystem of banks, card networks, tech platforms, and logistic companies. Over the past three years, we have signed over 40 partnership agreements with players across the ecosystem. FinTech can help all players in the ecosystem to reach new clients and customers and expand globally.

PayPal runs on top of the existing banking and credit card infrastructure, aggregating disparate financial services in the PayPal wallet and providing consumers with choice of how they wish to pay.

Partnerships between traditional financial services companies and FinTech firms are now becoming commonplace. In a survey of 70 executives at UK-headquartered financial services companies, 25 per cent reported that they had engaged in a joint venture with a FinTech in the past 3 years, and nearly 50 per cent stated that they planned to engage in a joint venture with a FinTech in the next three years.ⁱⁱ The benefits of these types of partnerships for customers is clear.

7. How should Australia take a prominent role in supporting and developing international blockchain standards? - How can the FinTech and RegTech sectors link into the Australian digital identity ecosystem reforms?

Blockchain is a global technology and would benefit from international standards. Blockchain technology remains in its early days and a multi stakeholder model for setting standards is likely the best solution in the near term. The Australian government and private sector should engage with global multi stakeholder bodies that are working on blockchain standards. Increased engagement from governments and large institutions can help to build security as the fundamental focus of blockchain and help to build trust in the future of the architecture.

8. In addition to traditional financial services, which sectors of the Australian economy could benefit most from the integration of innovative FinTech and RegTech technologies?

Retail will likely benefit tremendously from continued adoption of FinTech and RegTech. E-commerce is a rapidly growing sector in Australia and consumers that use e-commerce tend to benefit from lower prices and greater selection. Businesses that use e-commerce tend to benefit from great growth and an increased consumer base. As FinTech continues to take hold, it can help to grow the usage of e-commerce and increase trust in the e-commerce ecosystem. FinTech can also help to reduce the problem of retail fraud by leveraging advanced data analytics and machine learning to identify fraud and stop it before it can lead to losses.

9. How can technology solutions be used to improve access to financial and other services for geographically isolated or other marginalised groups in Australia?

The availability of basic broadband access throughout Australia is critical; we support government measures to further underpin the availability of internet access even in the most remote parts of Australia, at affordable prices.

Only 1 in 3 Australians say that they feel financially secureⁱⁱⁱ and about 1 in 7 or 2.6 million Australians say they have no savings for an emergency^{iv}. Technology solutions can help Australia to earn extra income, better manage their money, and build towards financial security. Moreover, technology solutions can scale across Australia to reach those in more isolated areas.

10. What innovations from other countries could have a positive impact on the Australian FinTech industry?

The sandbox experiences in the UK and in other countries around the world show that, at a minimum, sandboxes have encouraged regulators to open their minds to valuable innovation, and has fostered cooperation between innovators and regulators to embrace necessary norms and user protections as part of their design terms. This can only serve to promote a better ecosystem.

Other countries have setup "Innovation Academies" gathering industry experts, competent authorities (including data protection and cybersecurity authorities) and consumer organisations to share practices and discuss regulatory and supervisory concerns with government. Greater cooperation between the industry and regulators is essential for the continued growth of the Fintech and RegTech sectors.

The Open Banking experience in Europe, through the Payment Services Directive 2, could serve as a model for how Australia can implement its Open Banking initiative. The use of secure APIs and the creation of tiered regulatory requirements has enabled the regime to be both efficient and safe.

11. Are there any pitfalls Australia can avoid in growing its FinTech industry by learning from international experience?

The response to the threats of privacy, security, and seeming lack of control over FinTech in some countries has been to force providers to localise their services. The localisation of data is challenging for FinTech because the Internet is designed to allow data to flow freely.

FinTech is designed to be global from day one. The Internet enables the smallest FinTech player to instantly access customers around the world. But increased protectionism leading to policies of localisation threaten to undermine the growth potential for innovation in the FinTech arena. Australia should continue to avoid localization mandates in the FinTech arena and instead should focus on activity-based and risk-based approaches to regulation.

12. How can Australia take advantage of its geographical proximity to the rapidly growing markets in the Asia-Pacific and increase its financial services exports in the region?

The cross-border provision of FinTech services is challenging in Asia-Pacific. There is regulatory fragmentation in several areas (e.g. banking, credit, AML, etc.). There are major growth markets in the region that would benefit from collaboration with Australia on regulatory harmonisation. By aligning on regulatory issues, there is a far greater likelihood that Australian FinTechs can gain a foothold in some of these growth markets.

13. Should Australia seek more formal international FinTech agreements? Are there particular countries that Australia should look to for partnership?

The FinTech bridge between Australia and the UK is an excellent first step in the internationalization of FinTech cooperation. There are several other countries in Asia, Europe, and the Americas that would make sense for FinTech arrangements. The key focus for these arrangements should be some type of passporting system or harmonization whereby regulatory approval in one market can be relied upon to enter the other market. Such a cooperation regime will reduce regulatory burdens while maintaining high standards.

SUMMARY OF RECOMMENDATIONS

1. Creating a secure, government- issued digital identity framework linked to an electronic know your customer (e-kyc) could greatly improve the ecosystem for electronic payments. The Digital Transformation Agency's efforts in this space are an exciting development for PayPal.
2. Australia should also consider "risk-based" proportional authorisation, which is the idea that where the rules and regulations that apply to you should depend on the level of risk of your service.
3. Creating interoperability through passporting regimes is the ideal method for enabling FinTech to develop. An example of a successful model comes from European Union where an entity regulated in a single market in the EU can passport their regulatory status into other countries that are part of the Union. This model would enable far more rapid scaling of innovative and beneficial financial services solutions.
4. The Australian government and private sector should engage with global multi stakeholder bodies that are working on blockchain standards. Increased

engagement from governments and large institutions can help to build security as the fundamental focus of blockchain and help to build trust in the future of the architecture.

Please do not hesitate to contact Steven Chan, Regional Head of Government Relations for Asia Pacific if you have any questions or feedback in relation to the positions outlined in this submission.

Sincerely,

Neil Matthews
Chief Executive Officer
PayPal Australia

ⁱ <https://www.forbes.com/sites/forbestechcouncil/2018/07/10/know-your-customer-kyc-will-be-a-great-thing-when-it-works/#5b0cfe868dbb>

ⁱⁱ Mayer Brown, The ABC of FinTech: Acquisitions, Brexit and Collaboration, (November 2016)

ⁱⁱⁱ https://www.unimelb.edu.au/_data/assets/pdf_file/0005/3145613/Consumer_Research_Report.pdf

^{iv} <https://www.news.com.au/finance/australians-are-leaving-themselves-extremely-vulnerable-by-having-no-cash-reserves-for-a-rainy-day/news-story/523e8eed8cc0f5be988b785010723c3>