



11 September 2007

Head of Payments Policy Department  
Reserve Bank of Australia  
Sydney NSW 2001

By email: [pysubmissions@rba.gov.au](mailto:pysubmissions@rba.gov.au)

Dear Sir

### **2007/08 Review of Australia's Payments System**

Our submission on the Bank's review is set out below.

**What is PayPal?** The PayPal Service is a global online person to person (P2P) or person to merchant (P2B) payment service currently available in 190 countries (including Australia), permitting any Australian resident with an email address and a valid credit card, debit card or bank account to securely, conveniently and cost effectively send and receive payments within Australia or worldwide.

**How is PayPal regulated?** In Australia, PayPal is regulated by APRA as the provider of a purchased payment facility (*PPF*) under the *Payment Systems (Regulation) Act 1999* (Cth) (*PSRA*) and is licensed as an ADI under the *Banking Act 1959* (Cth) purely for the provision of its PPF. PayPal cannot describe itself as a bank, nor can it make loans or pay interest on deposits. Unlike other PPF providers regulated under the PSRA, PayPal does not issue cards of any type, including stored value cards or prepaid cards. PayPal is also the holder of an Australian Financial Services Licence and is subject to the financial services laws in Australia.

#### **How does PayPal work?**

- The PayPal Service is a "closed loop" service, which sits on top of the existing Australian banking and credit card infrastructure, typically used for low value transactions, with all transactions flowing through a single global database connected to the banking system and card processing system at both the front end (funds in) and backend (funds out) of a transaction. PayPal is a facilitator of online payments for individuals and small businesses predominantly. Both the sender (or purchaser) and receiver (or merchant) of an online payment are required to open a PayPal account. Receivers are able to display "PayPal" as a payment option on their website or listing, if an eBay type transaction. By accepting "PayPal", merchants in effect are able to receive payments from a purchaser in the manner in which the purchaser has designated in their PayPal account. This, at the purchaser's option, may be bank transfer, credit card, debit card, pre-paid card, or via an existing PayPal balance. Payments are placed in the merchants' PayPal account and may be withdrawn by the merchant at anytime through a designated bank account established by the merchant.
- The PayPal Service is a "transparent" service. Through the PayPal website, both individuals and businesses can see the fees applicable to a transaction. Merchants of any size can easily integrate PayPal as a payment option into their website.



- The PayPal Service is a “cost neutral” payment option. PayPal does not charge fees to senders of Payments. The preferred funding source is determined by the purchaser’s choice, rather than the merchant. At anytime, a purchaser may go into the PayPal website and change their preferred payment mechanism. This type of system creates a cost neutral option for individuals shopping online. The PayPal Service does not prefer any one type of credit card (Visa, MasterCard), nor one type of debit card, or even bank account, however, the PayPal Service is dependent upon, and works within, the traditional Payment System.

#### **What are the benefits of PayPal?**

- PayPal benefits both the sender and the receiver of payments. The PayPal Service is an alternative cost effective online payment mechanism for individuals and small businesses. It enables online businesses and individuals who would otherwise not be able to accept credit/debit card payments or bank funded payments to accept such payments in a more efficient and less costly manner. PayPal through its existing credit/debit card processing arrangements and bank agreements is able to consolidate the many relationships a typical individual or small business would be unable to enter into independently due to cost and inaccessibility in a simple package at a set price. So, though PayPal offers what could be seen as a payment service, it is truly a user of the traditional Payment Systems consolidating multiple relationships into an online package for use by non-typical merchants.
- PayPal also enables the sender of an online payment to choose the manner of such payment rather than being required to pay only with those credit cards, debit cards or card types accepted by the merchant and to do so without differing fees based upon payment type. PayPal has relationships with multiple card companies including: Visa (credit and debit cards) and MasterCard (credit and debit cards). In addition to credit/debit card payment options, transactions can be funded through bank account funding. Senders, or purchasers, do not pay fees for making payments through PayPal. So, although PayPal sits as a payment option for purchasers, what it provides to the online payment market is the freedom for the sender of funds to choose the payment method, including payment methods that traditionally are not available online.
- PayPal offers the consumer a low-cost, low-risk payment system alternative, with a comprehensive audit trail of electronic transactions that can be traced to source.

**How does PayPal interact with traditional Payment Services?** When PayPal customers fund a PayPal payment with their credit or debit card regardless of whether it is a P2P or P2B payment, PayPal pays a merchant fee to its credit/debit card processor. The level of this fee is agreed through a standard processor agreement between PayPal and its credit/debit processor (Acquirer), based on interchange rates set by the credit/debit card association which the processor must remit to the customer’s credit or debit card issuer. PayPal remains as the merchant of record with a relationship with an acquiring bank.

**How do interchange fees affect PayPal?** Accordingly, while there are no interchange fees applicable to merchants in the PayPal Service itself, the underlying costs associated with the operation of the PayPal Service are directly affected by interchange fees. Increased



interchange fees increase the cost to PayPal of providing its services to merchants and individuals as PayPal is the merchant of record.

**Conclusion.** Having regard to the fact that the PayPal Service is a "closed loop" service which sits on top of the traditional payment and banking systems, and is indeed a "user" of the systems sought to be regulated by the Reserve Bank of Australia, PayPal maintains that further regulatory reach is unwarranted.. PayPal has become an important alternative for online shoppers and online merchants, with over three million registered users as of October 2006 in Australia alone and 153 million registered users worldwide.

On the matter of surcharging, PayPal argues that the RBA's removal of the "no surcharge" rule in established payment systems (with no upper limit defined) has allowed merchants to divert system cost to consumers. Consumers are commonly not aware of the level of surcharge and this has led to examples of excessive charges, particularly among merchants that have market dominance or in regional areas where consumers do not have a choice of merchant.

Moreover, the RBA's prohibition on "no surcharge" rules will impede the entry of new competition into the domestic market because prospective entrants will not be able to use "no surcharging" as a mechanism to build a market with network benefits. If subjected to no surcharging rules, payment system alternatives such as PayPal would not have the opportunity to grow and develop in the manner that incumbents have benefited.

PayPal would be pleased to provide the Bank with further information, whether in connection with the Bank's studies on resource costs associated with different methods of payment and how various payment methods are used by consumers in different situations, or otherwise.

Yours faithfully

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