

TESTIMONY OF

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Is Cash Still King? The Rise of Mobile Payments

PRESENTED

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Introduction – Who is PayPal

Chairwoman Waters, Ranking Member McHenry, Chairman Lynch, Ranking Member Emmer, and members of the Task Force, I would like to thank you all for giving PayPal Inc. the opportunity to testify today on the important topic of mobile payments. Since 1998, PayPal has been at the forefront of innovation in mobile payments. PayPal operates an open, secure and technology-agnostic digital payments platform that gives our over 300 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.

Through a combination of technological innovation and strategic partnerships, PayPal creates better ways to manage and move money. We offer people and businesses choice and flexibility when they send payments and receive payments. Whether sending money to friends and family through apps like PayPal, Venmo, and Xoom, or engaging in e-commerce, more and more people are using their smartphones to make purchases, receive payments and manage their accounts. Our technology is giving more people and businesses access to the global market, and financial services tailored to their specific needs.

We enable peer-to-peer, or P2P, payments via PayPal, Venmo and Xoom. In Q3 of 2019, our collective P2P volume was \$51B and represented 28% of our total payment volume. In particular, Venmo has seen enormous growth since it launched in 2009 as a fee-free, digital way to move money between friends in the US.ⁱ As of August 2019, Venmo had 40 million users.ⁱⁱ Venmo's contribution to PayPal's total payment volume stood at 14%. According to a survey done in 2017, of the 65% of young Americans that did use payment apps, more than two-thirds — 68% — said they used Venmo most often.ⁱⁱⁱ

The Venmo app pioneered the idea of social payments by allowing users to post memos and emojis attached to transactions where you can see friends paying one another for a meal out, or roommates sending money to each other for utilities and rent. While this social aspect is what makes Venmo unique, it is imperative to note that users can determine their privacy settings and have the option to make transactions “private” so that they appear only to the sender and the recipient. Being able to send secure and easy P2P payments across the country via a few taps on the phone is an important improvement in people's lives. And, what began as a fun way to pay friends back for everyday expenses has now become an option to pay at millions of retailers.

The ability to use Venmo is not solely limited to purchases and payments within the e-commerce ecosystem. The Venmo Card enables users to spend their Venmo balance in-store and online anywhere that Mastercard is accepted in the U.S. The card is ATM friendly. Venmo's functionality offers tools to make people's lives easier. The app includes a tool that automatically calculates suggested tip amounts, so there's no need to crunch the numbers on a calculator or worry about over or under tipping. Also, users can easily split and share the payment with friends in the Venmo app on a single purchase such as dinner at a restaurant.

Xoom is a pioneer in international digital remittances, and a fast and secure way to send money, pay bills and reload phones for loved ones globally. It allows consumers to use a mobile device

or PC to send money to recipients for cash pickup or directly into their bank accounts, typically in minutes, to more than 160 countries globally. Xoom users can also save their family the trouble of carrying cash and waiting in line, by taking care of the bill payments. Most bills will be paid typically within minutes. These remittances serve as a lifeline for many people around the world and are used to pay for everyday needs like utility bills, healthcare, mobile reload, and education costs, as well as emergencies. The largely cash-based system of sending money across borders is full of paperwork, high fees, standing in line and an ever-present uncertainty of when, and if, the money will arrive. By providing fast and more secure payment options for customers to seamlessly and securely send money across borders by going online or using a mobile device, PayPal and Xoom are helping to expand and improve the financial health of millions of people worldwide.

In November 2019, Xoom announced an expansion of its services to give customers in the United States the ability to send money to recipients within the U.S.—for the first time. Through collaborations with Walmart and Ria, people in the U.S. can now use Xoom to send money fast for cash pick-up typically in minutes at nearly 5,000 store locations across the country.

As the economy digitizes, PayPal as a two-sided network, will continue to drive consumer adoption and merchant acceptance of mobile payments. PayPal’s mobile app is localized in over 100 markets and 26 languages. We also help merchants, particularly small merchants, optimize their checkout pages for mobile access.

Finally, we can utilize data from mobile payments, in partnership with a financial institution, to underwrite working capital loans for small businesses. This access to finance is key to the growth of small businesses. 70% of PayPal Working Capital loans go to the 10% of counties in the US that have lost 10 or more banks since the financial crisis. Moreover, 32% of PayPal Working Capital loans go to women owned businesses, whereas the average from traditional financial institutions is just 16%.

By leveraging technology to make financial services and commerce more convenient, affordable, and secure, the PayPal platform is empowering over 300 million consumers and merchants in more than 200 markets to join and thrive in the global economy. In Q3 of 2019, 43% of the \$179 billion total payment volume we processed were made on a mobile device.

The Power of Mobile Payments

The mobile phone has transformed nearly every aspect of our lives. We use it to communicate with family, to read the news, order a cab, find a hotel, and engage in payments. The growth of smartphones over the past decade has been incredible. In 2011, only 35% of Americans owned a smartphone; the percentage grew to 81% by 2019.^{iv}

Payment technologies have evolved throughout history – checks and bills of exchange were the innovation of 1750s, credit cards were the innovation of the 1950s, ACH in the 1960s, and debit cards in the 1970s. Since the dawn of the Internet revolution in the 1990s, online and mobile payments have transformed the payments industry.

At the end of 2018, 3.6 billion people were connected to the mobile internet; which means almost half of the world's population are mobile internet users.^v The ubiquity of smartphones has made it an ideal platform over which robust payment solutions are offered. While money is a complex and very personal aspect of our lives, essentially every dollar earned or spent in every country follows the same pattern: it is acquired, it is managed, and it is sent.

For most of history, acquiring, managing, and sending money were interconnected in concept but disparate in reality. We took different actions, used different services, and visited different places, depending on where we were in the process and what funding instruments were used. However, mobile has the power to bring them together and make them available at our fingers, along with the power of customization and freedom. It is now possible to receive, manage, and send money using apps on a single mobile device, consolidating and simplifying disparate tasks that have historically been costly, in terms of money, time, and mental bandwidth.

Mobile payments offer an unprecedented level of seamlessness and convenience. The PayPal One Touch technology enables businesses to provide a quick and easy checkout method for customers. Users can transact without pop-up windows, redirection or having to type or retype a username, password or 16-digit credit card number, all in a secure manner. In addition to enabling remote transactions, mobile payments can also be a more convenient option for in-person transactions, relative to cash. Mobile devices can be used for payments at the point of sale through a simple touch.

Mobile payments have been growing rapidly in importance for everyday payments. 17% of businesses earn the majority (more than 50%) of their revenue through the mobile channel today. 32% of businesses expect mobile to represent at least half of their total revenue by 2020.^{vi}

Mobile devices are the new hardware foundation upon which a full suite of financial services can be offered. There are countless opportunities to improve financial services like bill payment, government disbursement, consumer credit, and small business financing through the data derived through mobile payments.

At PayPal, we regard fighting cybercrime as a strategic business priority, and we invest heavily in keeping our sites and services as safe and secure as possible. PayPal's philosophy on cybersecurity has a strong focus on customer data protection. Everything we do around security is focused on our commitment as the "secure way to pay and be paid." It is important to approach security across the industry, helping providers to keep their systems secure by analyzing data in real-time to understand behavior alongside static data to help verify identity and protect consumers.

Security has been front and center throughout the development of mobile payments, leading to adoption of innovations such as the tokenization technology, which reduces the number of entities that have access to sensitive financial data. PayPal has been a pioneer of tokenization technology. Tokenization substitutes a person's sensitive financial information with a series of non-sensitive numbers that confirm to the business that a payment is authentic, helping to minimize the likelihood and impact of data breaches as well as reduce fraud.

Service providers can also leverage key information from the mobile device to improve identification, authentication, and fraud reduction. PayPal is a founding member of the Fast IDentity Online (FIDO) Alliance whose mission is to find new methods of authentication that move away from passwords and towards biometrics (fingerprint, etc.). Moreover, with a PayPal transaction, should something go wrong with a purchase, e.g. an item doesn't arrive, or it doesn't appear significantly the way it was described, then PayPal covers them under Purchase Protection or Free Return Shipping for eligible purchases. These services are made possible in large part due to mobile payments data that we use for fraud and risk management services.

PayPal also engages and partners with law enforcement proactively and reactively to help stop illegal activities that leverage mobile payments, while also catching the bad actors that have committed crimes and are under investigation. This ability to leverage the mobile payment system to stop illicit payments is a marked distinction from a payments system that is predominantly cash based.

Finally, mobile payments hold the power and promise to improve people's financial health. Tasks that many take for granted like cashing a check, paying a bill, and sending money to a loved one are inconvenient, expensive, unsafe—and sometimes impossible. The advancement of mobile payments has important implications for unbanked, underbanked, and financially unhealthy individuals and communities.

The 2017 FDIC survey of unbanked and underbanked households found that about 8.4 million households are unbanked.^{vii} According to research from Pew, the majority of the unbanked have a smartphone.^{viii} The reason for the failure to use mobile payments is not necessarily lack of access. The most significant barrier to mobile payments for unbanked consumers is their poor compatibility with the way in which unbanked consumers often earn and use money.^{ix}

Nearly 25 million US households are underbanked, meaning they use alternative financial services like payday lenders and check cashers alongside their formal financial services.^x To manage their financial lives, the underbanked use instruments such as money orders, check cashing, international remittances, payday loans, refund anticipation loans, rent-to-own services, pawn shop loans, or auto title loans.^{xi} Professor Lisa Servon's research has shown that the underbanked use these instruments because they are often more timely, more immediate, lower cost, and more convenient than traditional products.^{xii}

Regardless of banking status, a large portion of the U.S. population is financially unhealthy. Nearly 70% of Americans have less than \$1,000 in savings.^{xiii} Four in five Americans say they live paycheck to paycheck.^{xiv} Faced with a \$400 emergency expense, 40% of all Americans would not be able to pay, and would need to sell something or rely on credit.^{xv} And countless hours have been wasted just for low- and moderate-income individuals to pay their bills.

Mobile payments technology allows customers to make online and point-of-sale purchases, pay bills, and send or receive money from their smartphones via web browsers, apps, or text messages. Mobile payments offer a low cost, safe, fast, and convenient way of managing and moving money, and that has the potential to improve the financial health of consumers who are underserved by the traditional financial system. For example, giving people access to their

money instantly via mobile can actually help quite a bit in reducing fees and late payments. Access to credit during cash flow challenges is another area where mobile payments can make a big difference. Finally, remittances and P2P payments at a distance can be made far more efficient and lower cost.

Xoom's services potentially benefit more than 44 million foreign-born people in the U.S. who send remittances to family and friends in their home countries.^{xvi} Sending money overseas with Xoom/PayPal costs on average less than half the cost of traditional remittances.^{xvii} Our analysis suggests that digital remittances are well on the way to achieving the UN Sustainable Development Goal of lowering remittances costs to less than 3%.^{xviii} Moreover, mobile payments can greatly reduce the time cost of sending a remittance, which typically takes over 30 minutes on average to send.^{xix} When sending a digital remittance through Xoom by depositing money to a bank account, it typically takes less than 3 minutes. That is 27 minutes saved on average every time someone sends a remittance, around 10 days given back to that person over the course of their life, nearly 300 million hours and almost \$5 billion in time-cost in aggregate that could be put to better use.

By harnessing the power of mobility to bring the financial institutions to the consumer, mobile technologies can serve as a tool for improving financial health. Access to institutions and funds, as well as clarity of account information, can disproportionately impact poorer individuals. By offering a more convenient and less expensive way for managing and moving money, without the constraints of geography and hours, mobile technologies like digital wallets and person-to-person (P2P) payments can help the underbanked take more control of their financial lives.^{xx} For example, consumers can easily utilize different payment options, which is important for managing costs at the margins. Moreover, one of the features of mobile payments is automatically tracking and displaying a clear record of how a user is spending money, thereby enabling better decision-making.

There is also an opportunity for mobile payments to form a baseline architecture upon which other value-added financial services can be offered in an innovative and prudent manner. PayPal has built successful products and partnerships for peer-to-peer, remittances, credit, savings goals and wealth management. PayPal has partnered with several players to provide U.S. consumers with access to affordable and convenient financial solutions for the underserved. The PayPal Cash Mastercard allows unbanked and underbanked customers to pay bills and shop anywhere that Mastercard is accepted without monthly fees. "Direct Deposit" allows customers to load all or part of their paychecks directly into PayPal. "Money Pools" help groups using PayPal to collectively pool funds for shared items or activities. "Goals" help people plan ahead and organize their funds for future spending. Integration with Acorns allows customers to easily transfer funds from their PayPal to their Acorns account and track investment performance. These products leverage technology to lower costs, increase access, enhance security, maximize convenience, and improve financial health of our customers. Because of the proliferation of mobile technology and the digitization of financial transactions, we have entered into a period where financial services can be transformed at an unprecedented pace and scale.

Digital payments are not made in silos. Partnerships across the industry, platforms and networks serve as electronic paths and highways that connect customers in ways that benefit them. For example, our partnership with Citi allows institutional clients of Citi to make payments into their customers' PayPal digital wallets. Also, we partner with Visa for a more seamless payment experience for Visa cardholders and will offer greater choice for how consumers pay with PayPal and Venmo wallets. And we count several major technology companies as partners.

In order to modernize and make inclusive the mobile payments system, we work together with both traditional financial services and startups to enable businesses and consumers to benefit from lower cost and more efficient services. As PayPal has evolved, our biggest shift has come by realizing that payments itself is a trillion-dollar industry and financial services is far bigger; no one company should or will ever own that whole market. Therefore, PayPal has fully embraced an ecosystem partnership strategy. We believe that fintech is not about disruption; it is about value creation 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. And, we believe that this value creation comes through partnership. While mobile has created completely new avenues and channels to democratize finance, it is only through partnership that we can more fully maximize those opportunities.

Cash

Although use of non-cash payments, including mobile, has been growing in recent years, cash still remains a major portion of the payments ecosystem in the United States. The 5th Federal Reserve Diary of Consumer Payment Choice conducted in 2019 found that consumers used cash in 26 percent of transactions. The share of cash use among individuals under 25 years old is the highest of any age group. Cash continues to be used extensively for small-value purchases, representing nearly 50 percent of all payments under \$10, and 42 percent of payments less than \$25. In contrast, cash is used for approximately 10 percent of payments \$25 and higher.^{xxi}

Cash is a ubiquitous form of payment, but while it may appear costless to transfer, there are high costs associated with cash usage. Sixty-five percent of the unbanked earn less than \$25,000 a year, and these low-income consumers incur additional costs and risks because they lack access to mainstream banking services. For example, 20 percent of unbanked consumers reported having cash lost or stolen.^{xxii} A study of low-income Los Angeles area households found that the average unbanked consumer lost the equivalent of nearly two weeks of household expenses when cash was lost or stolen.^{xxiii}

Professor Kenneth Rogoff of Harvard University authored a book entitled "The Curse of Cash" in which he documented several costs associated with cash.^{xxiv} Cash is deeply implicated in tax evasion, which costs the US federal government some \$500 billion a year in revenue. The drug trade, bribes, human trafficking, and terrorism are all fueled by cash payments. When Mexican drug lord El Chapo was arrested more than \$200 million in cash was found on the premises; the drug trade globally is estimated at \$600 billion. Cash can also be used to facilitate corruption; the scale of bribes is estimated at \$2 trillion annually. Cash is the currency of choice to fund terrorism; the official currency of ISIS is the US dollar and the organization has annual

expenditures of between \$1 and 2 billion per year. Counterfeiting, though a small problem in the grand scheme, nevertheless exists and results in harm.

Mobile payments present a tremendous opportunity to reduce reliance many of the costs associated with cash. We don't predict the death of cash over the next decade or two and we believe that consumers should have choice in their payment options. We are working diligently to make sure that the value proposition of digital payments vastly exceeds the value proposition of cash for every member of society.

The Role of Policy

To reflect the move towards mobile, payments policy will need to continue to evolve.

We urge policymakers to collaborate with industry to ensure regulation of mobile payments meets the goals of consumer protection, security, and healthy industry innovation. Responsible innovation can and ought to develop with consumer protection, security and safety at the core.

The key is to put in place regulations that are smart and technology-neutral, such that regulations are created based on performance rather than the type of technology. Regulations are most successful if they consider divergent risks posed by new offerings and tailor requirements that are proportionate to the risk being posed. Not every innovation is inherently riskier, and sometimes innovation can lower risks.

Moreover, from the perspective of security, mobile payments may be considered a good tool for reducing reliance on the use of anonymous cash. Mobile payments can aid in reducing Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT) risks due to improved transaction monitoring and restrictions. Mobile payments can be enabled via effective and proportionate applications of AML/CFT regulatory frameworks.

We also urge policymakers to consider the connection between broadband and mobile broadband deployment and its impact on access to mobile payments for members of the unbanked, underbanked, and financially unhealthy individuals and communities. While many unbanked and underbanked families have access to the Internet, maintaining phone service is often a financial hardship for this population. The unbanked are nearly twice as likely as banked consumers to suspend or cancel their cellphone plans because they were too expensive. Among smartphone owners with limited data plans, nearly half of unbanked consumers reach their data limits most or some months, which indicates a high amount of use. About 7 percent of U.S. consumers rely exclusively on their smartphones for accessing the Internet.^{xxv}

Households with incomes under \$30,000 annually, which include about 60 percent of unbanked consumers, are almost twice as likely as the general population to be smartphone-dependent. Unless smartphone owners with limited data plans can access a Wi-Fi network or purchase additional data at an affordable rate, they are unable to use mobile payments technology regularly. As a result, mobile payments use is significantly lower among the unbanked: About 39 percent of unbanked smartphone owners have ever made a purchase, paid bills, or sent or received funds using mobile payments technology compared with 64 percent of banked

smartphone owners.^{xxvi} Since a majority of the unbanked population in America has a smartphone, that represents tremendous opportunity to reach out to these unbanked customers through digital tools.

Policy can also play a role in helping to improve the mobile payment use cases for unbanked and underbanked consumers. Government payments can be disbursed directly into electronic formats. Government bill payments can incentivize electronic payment acceptance. Micro-entrepreneurs in low-income neighborhoods can be incentivized to move towards electronic and mobile payments, which would create a virtuous cycle for consumer adoption of mobile payments. All of these incentives can be created in partnership with the private sector to enable greater reach and a balanced equitable solution set.

Conclusion

Fueled by a fundamental belief that having access to financial services creates opportunity, PayPal is committed to democratizing financial services and empowering people and businesses to join and thrive in the global economy. We believe that individuals, families, small businesses and communities are going to be the economic winners from the continued melding of mobile technology and payments as well as increased competition.

Thank you again for the opportunity to address the Task Force on this important and timely topic. I look forward to answering your questions.

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