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IS STARBUCKS A BANK? HOW THE BILLIONS CONSUMERS UPLOAD ONTO STARBUCKS CARDS SHOULD BE REGULATED

❖ Note ❖

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I. INTRODUCTION

As technology has continued to advance, so have company reward programs. In 2021, Starbucks customers loaded $11 billion onto mobile Starbucks Cards,[1] accounting for almost half of all Starbucks sales.[2] The amount of money consumers have loaded onto their mobile applications to prepay for their coffee orders has allowed Starbucks to overtake most banks in terms of assets.[3] "85% of US banks have less than $1 billion total in assets, illustrating the major player Starbucks has become in this space."[4] Should the billions of dollars that consumers have uploaded onto Starbucks Cards be regulated by the federal government?

Part II of this Note discusses the history of the Starbucks Reward System and how it is currently regulated. Part II also addresses how different traditional banking categories are regulated. Part III discusses the category into which Starbucks Cards best fit and how this impacts the way they should be regulated. Part IV will provide a recommendation on whether the government should insure Starbucks Cards and will give advice to consumers on the best ways to protect themselves.

II. BACKGROUND

Starbucks released its first rewards program in 2008 and launched mobile payment in 2011.[5] The Starbucks reward program has continued to grow, and in 2021, more than $11 billion was loaded onto Starbucks Cards.[6] In addition, a large amount of the money deposited onto Starbucks

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1 Mary Meisenzahl, *Starbucks Customers Have More Than $1 Billion Ssitting on Gift Cards*, BUS. INSIDER, (May 4, 2022, 1:50 PM), https://www.businessinsider.com/starbucks-says-over-1-billion-is-sitting-on-cards-2022-5.

2 Lisa Moyle, *Starbucks: Banking & Serving Coffee*, FUTURE IDENTITY FIN., (July 19, 2022), https://fttembeddedfinance.com/starbucks-banking-serving-coffee/.

3 *Id.*

4 *Id.*

5 Peter Bondarenko & Melissa Petruzzello, *Starbucks*, BRITANNICA, https://www.britannica.com/topic/Starbucks (last updated Mar. 3, 2023).

6 Meisenzahl, *supra* note 1, at 1.

Cards ends up going unused.[7] In 2019, based on historical data, Starbucks calculated that it generated $141 million in revenue from unused deposits.[8]

The structure of the Starbucks rewards program incentivizes consumers to load money onto Starbucks Cards. When a Starbucks rewards member uses another form of payment, such as cash or a credit/debit card, they earn one Star per $1 spent.[9] However, when a Starbucks rewards member uses a Starbucks Card to pay, they earn two Stars per $1 spent.[10] Consumers are so persuaded by this incentive that Starbucks itself sells more gift cards than all other companies combined.[11]

According to the Starbucks Card Terms and Conditions, "the dollar value that consumers load onto their Starbucks Card is a prepayment for the goods and services of participating stores."[12] Money that has been uploaded onto a Starbucks card is nonrefundable and cannot be redeemed for cash.[13] In addition, the "value of the Starbucks Card is not insured by the Federal Deposit Insurance Corporation ("FDIC"), nor does it earn interest."[14]

Starbucks Cards are gift cards. Gift cards are regulated by the Credit Card Accountability Responsibility and Disclosure Act of 2009.[15] The Act requires that gift cards do not expire until at least five years after they have been activated and sets limits on inactivity fees.[16] In addition to federal legislation, many states have passed statutes regulating gift cards.[17] Ten states require that issuers of gift cards allow purchasers to redeem their gift cards for cash, but generally only if the remaining balance is less than $5.[18]

As the public has started to learn about the amount of money consumers are uploading onto Starbucks Cards, Starbucks has often been compared to a bank.[19] In addition, the money loaded onto Starbucks Cards could be considered an investment or loan.[20] In the United States, banks are regulated by both the federal government and individual states.[21] The government imposes restrictions on how traditional banks can invest customer deposits.[22] Most banks are insured by the Federal Deposit Insurance Corporation ("FDIC"), which is backed by the full faith and credit of the

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[7] *Id.*

[8] Neil Patel, *How Starbucks Quietly Benefits From its Most Passionate Customers*, MOTLEY FOOL, (Jun. 18, 2022), https://www.fool.com/investing/2020/06/17/how-starbucks-quietly-benefits-from-its-most-passi.aspx.

[9] *Earning Stars*, STARBUCKS, https://www.starbucks.com/rewards#:~:text=Earning%20Stars&text=Earn%201%20Star%20per%20%241,pay%20directly%20through%20the%20app. (last visited Mar. 17, 2023).

[10] *Id.*

[11] *See* Meisenzahl, *supra* note 1, at 1.

[12] *Starbucks Card Terms & Conditions*, STARBUCKS, https://www.starbucks.com/terms/manage-gift-cards/ (last visited Mar. 17, 2023).

[13] *Id.*

[14] *Id.*

[15] Heather Morton, *Gift Cards and Gift Certificates Statutes and Legislation*, NCSL, https://www.ncsl.org/financial-services/gift-cards-and-gift-certificates-statutes-and-legislation (last updated Apr. 22, 2016).

[16] *Id.*

[17] *Id.*

[18] *Id.*

[19] Jason Kottke, *Starbucks Is a Bank that Sells Coffee*, KOTTKE, (Feb. 3, 2022), https://kottke.org/22/02/starbucks-is-a-bank-that-sells-coffee.

[20] *See* Kevin Mwanza, *Starbucks Customers Have a Balance of $1.4 Billion on the App, Interest-Free Loan*, MOGULDOM NATION, (Jun. 9, 2021), https://moguldom.com/357346/starbucks-customers-have-a-balance-of-1-4-billion-on-the-app-interest-free-loan/.

[21] Adam Barone, *How Banking Works, Types of Banks, and How to Choose the Best Bank for You*, INVESTOPEDIA, https://www.investopedia.com/terms/b/bank.asp (last updated Aug. 19, 2022).

[22] Patel, *supra* note 7, at 2.

U.S. government.[23] The FDIC does not insure investments,[24] but the Securities Investor Protection Corporation ("SIPC") does.[25] The SIPC does not insure losses incurred as a result of market activity or fraud, but it does cover the losses of investors' accounts incurred by the bankruptcy of their broker or dealer.[26] Loans, on the other hand, are not insured by the government.[27] However, most lenders create their own insurance by securing their loans.[28]

III. ANALYSIS

A. Is Starbucks a Bank?

In 2021, $11 billion was uploaded by consumers onto Starbucks Cards.[29] This figure has led Starbucks to surpass the number of assets held by most banks.[30] In fact, 85% of banks in the United States have less than $1 billion in assets.[31] Starbucks has more assets than the majority of U.S. banks, and therefore, the first category that the company may fit into is a traditional bank.

"A bank is a financial institution that is licensed to accept checking and savings deposits and make loans. Banks also provide related services, such as individual retirement accounts (IRAs), certificates of deposit (CDs), currency exchange, and safe deposit boxes."[32] While Starbucks does take in substantial amounts of money, Starbucks is not licensed to accept deposits or make loans. In addition, Starbucks does not offer any other financial services that banks typically offer. Starbucks does not fit into the traditional definition of a bank.

B. Is Starbucks Receiving an Unregulated Investment?

The money loaded onto Starbucks Cards could be considered an investment in the company. "An investment is an asset or item acquired with the goal of generating income or appreciation."[33] Additionally, "[i]n general, any action that is taken in the hopes of raising future revenue can also be considered an investment."[34] A Starbucks Card is purchased with the goal of earning rewards faster. Technically, this could be considered income, because customers get free rewards, such as cups of coffee, for specific amounts of money they spend on their Starbucks Cards.

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[23] *Are My Deposit Accounts Insured by the FDIC?*, FDIC, https://www.fdic.gov/resources/deposit-insurance/financial-products-insured/index.html (last updated Mar. 14, 2023).

[24] Matthew Goldberg, *FDIC Insurance: What it is and How it Works*, BANKRATE, (Mar. 13, 2023), https://www.bankrate.com/banking/fdic-insurance/

[25] Mark P. Cussen, *Who Insures Your Investment in the Stock Market*, INVESTOPEDIA, https://www.investopedia.com/ask/answers/are-my-investments-insured/#:~:text=The%20element%20of%20risk%20is,the%20higher%20the%20potential%20return. (last updated Apr. 9, 2022).

[26] Goldberg, *supra* note 23, at 4; Cussen, *supra* note 24, at 4.

[27] Will Kenton, *Commercial Loan: What it Is, how it Works, Different Types*, INVESTOPEDIA, https://www.investopedia.com/terms/c/commercial-loan.asp (last updated Nov. 24, 2020).

[28] *Id.*

[29] Meisenzahl, *supra* note 1, at 1.

[30] *Id.*

[31] *Starbucks, a Bank that Sells Coffee! – The Epitome of Digital Wallets Strategy*, FIE-CONSULT, (Aug. 19, 2022), https://fieconsult.com/starbucks-a-bank-that-sells-coffee-the-epitome-of-digital-wallets-strategy/.

[32] Barone, *supra* note 20, at 4.

[33] Adam Hayes, *Investment Basics Explained with Types to Invest In*, INVESTOPEDIA, https://www.investopedia.com/terms/i/investment.asp (last updated Mar. 16, 2023).

[34] *Id.*

Even if the money was considered an investment, it would not be insured by the federal government. Consumers are not putting money onto their Starbucks Cards through a broker or dealer, which is a requirement for an investment to be one that the SIPC will insure.[35] Instead, this is a direct transaction between Starbucks and the consumer.

C. Are Consumers Giving Starbucks an Interest-Free Loan?

The money consumers deposit onto Starbucks Cards could be considered a loan to Starbucks. "A loan is when money is given to another party in exchange for repayment of the loan principal amount plus interest."[36] Most loans have interest rates, but they do not necessarily have to.[37] Starbucks customers load money onto their Starbucks Cards as a prepayment for their future coffee orders. When consumers upload money onto their Starbucks Cards, Starbucks is "essentially gaining access to an interest-free line of credit, one that equates to roughly 4% of the company's total liabilities."[38] Starbucks is then able to use this money to enhance their cash flow, decrease their working capital, and make investments into expanding their business.[39] Starbucks repays these customers when they purchase their coffee. A large amount of the money deposited onto Starbucks Cards goes unused.[40] In 2019, based on historical data, Starbucks calculated that it generated $141 million in revenue from unused deposits.[41] Therefore, Starbucks is not actually getting an interest free loan. Instead, the company is borrowing $11 billion a year at an effective rate of negative 10%.[42]

D. Where Does Starbucks Fit Best?

While Starbucks could theoretically fit into either the investment or loan category, the money on Starbucks Cards is best described as a loan to Starbucks. Out of the three categories, loans are the only one not insured by the federal government or the states individually. Instead, the government leaves it to private parties, including banks and other lenders, to protect themselves. While Starbucks is technically getting a $11 billion loan at an effective interest rate of negative 10%, Starbucks Cards are just gift cards. No other company has sold anywhere near the amount of gift cards that Starbucks does each year, but truthfully, any company's gift card sales could be considered a loan. The federal government has been regulating gift cards since 2009, and many states have additional regulations on gift cards. However, neither have shown an interest in insuring gift card purchases.

Banking accounts and investments are very distinguishable from the purchase of gift cards. In October of 1929, the stock market crashed, causing more than 9,000 banks to fail by March 1933.[43] "Congress took action to protect bank depositors by creating the Emergency Banking Act of

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35 Cussen, *supra* note 24, at 4.

36 Julia Kagan, *What Is a Loan, How Does It Work, Types, and Tips on Getting One*, INVESTOPEDIA, https://www.investopedia.com/terms/l/loan.asp (last updated Apr. 19, 2021).

37 *See* Lindsay VanSomeren & Jordan Tarver, *Should You Get an Interest-Free Loan?*, FORBES ADVISOR, https://www.forbes.com/advisor/personal-loans/interest-free-loans/#:~:text=Do%20Interest%2Dfree%20Loans%20Exist,as%20electronics%2C%20jewelry%20or%20furniture. (last updated Apr. 16, 2021, 2:25 PM).

38 Patel, *supra* note 7, at 2.

39 *Id.*

40 *Id.*

41 *Id.*

42 *Id.*

43 Robert Stammers, *The History of the FDIC*, INVESTOPEDIA, https://www.investopedia.com/articles/economics/09/fdic-

1933, which also formed the FDIC."[44] The federal government insures banks with the FDIC to prevent consumers from losing their entire life savings if their bank fails and closes. The SIPC was created under the Securities Investor Protection Act of 1970.[45] The SIPC "oversees liquidation of broker-dealers who go bankrupt, lapse into financial trouble, or if the assets of their customers go missing."[46] The SIPC "is not an agency, nor is it part of the United States government."[47] Instead, "it is an insurance."[48] The federal government created the SIPC because it was worried about people losing their entire college fund or retirement account if their brokerage went bankrupt. In contrast, consumers typically load relatively insignificant amounts onto their gift cards. In fact, Starbucks does not allow an individual to have more than $500 on a Starbucks Card at any time.[49] A loss of $500 is a small amount compared to someone losing their entire life savings, college fund, or retirement account. The amount of money on gift cards is very distinguishable from bank accounts and investments, and therefore, it is unlikely the federal government would have any interest in insuring it.

In addition, the federal government regulating Starbucks Cards is a slippery slope. If the government insures Starbucks Cards, it will be pressured to insure all gift cards. One problem with this is that it would be extremely difficult for the government to keep track of. The federal government would not step in to provide insurance until a business goes bankrupt, and it would be difficult to figure decipher who deserves to be paid back. In addition, it is likely that many people would only be owed extremely tiny amounts. For example, what would the government do about a consumer with sixteen cents left on a gift card they never intended to use? It seems like an extraordinarily complex and tedious task. Furthermore, small businesses are much more likely than large businesses to go bankrupt.[50] Small businesses are often not as technologically advanced, so insuring their gift cards would be even more difficult.

IV. RECOMMENDATION

Based on the above analysis, the federal government should continue to regulate gift cards to protect consumers. However, the government should not extend that protection to insure Starbucks Cards. First, individual consumers do not put enough money on their Starbucks Cards to require them to be backed by the full faith and credit of the federal government. Bank accounts hold individuals' life savings and investment accounts hold college and retirement funds, which gives the government a large incentive to make sure they are insured. In addition, the government has a strong interest in preventing financial crises. On the other hand, the money loaded onto Starbucks Cards is a small amount of money that an individual consumer has decided to deposit for their future purchases at Starbucks. A consumer can put as little as $5 on a Starbucks Card at any given time, making it likely that consumers are only uploading amounts they can afford to be without.[51]

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history.asp#:~:text=The%20Federal%20Deposit%20Insurance%20Corporation,of%20the%20nation's%20financial%20system. (last updated Mar. 15, 2023).

44 *Id.*

45 Kenton, *supra* note 26, at 5.

46 *Id.*

47 *Id.*

48 *Id.*

49 *Starbucks Card Terms & Conditions, supra* note 11, at 3.

50 *Why are Small Businesses More Likely to File for Bankruptcy?*, REINHERZ L. OFFICES, https://reinherzlaw.com/why-are-small-businesses-more-likely-to-file-for-bankruptcy/ (last visited Mar. 17, 2023).

51 *Starbucks Card Terms & Conditions, supra* note 11, at 3.

Second, the federal government insuring Starbucks Cards is a slippery slope. If the government insures Starbucks Cards, it will be pressured to insure all gift cards. In addition, there are other companies, such as PayPal and Venmo, that allow consumers to upload balances and are not insured.[52] PayPal and Venmo actually have a much more compelling need for insurance than Starbucks because they put all of their customers balances together and invest the money into liquid investments.[53] It would be impossible for the federal government to insure every mobile application that consumers have the ability to upload money onto. If the government goes down the path of insuring Starbucks Cards, it will be pressured to regulate all gift cards, as well as other companies, such as PayPal and Venmo, that have an even more compelling need for insurance than Starbucks Cards.

Consumers upload their money onto Starbucks Cards because they are happy with the return of earning rewards, such as free cups of coffee, for half the cost. The government should not interfere with the choices and judgments of individuals on how they wish to spend their money, especially when it equates to such a small amount of money per consumer.

The best solution is for consumers to protect themselves by being more informed when uploading money onto Starbucks Cards. One way that consumers can protect themselves is by not uploading too much money onto their Starbucks Cards at once. Consumers should only upload an amount of money that they will realistically spend in one month. In addition, consumers should ensure that they know the terms and conditions prior to uploading money onto their Starbucks Cards, or any other mobile application. For example, if an individual uploaded money onto a Starbucks Card and later needed that money back, they may be disappointed to find out that Starbucks Card cannot be redeemed for cash.

V. CONCLUSION

In conclusion, while it does seem unfair that Starbucks is getting a large loan that they are effectively earning interest on, the government should not step in and insure this money. The amount of money uploaded by each consumer is too little to be comparable to the other areas that the federal government chooses to provide insurance, and therefore, it should not be a concern of the federal government. Instead, consumers should be left to make these value judgments, and should take initiative on protecting themselves.

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[52] *Program Banks*, PAYPAL, https://www.paypal.com/us/legalhub/program-banks-tnc?locale.x=en_US#:~:text=FDIC%20insurance%20does%20not%20protect,failure%20of%20PayPal%20or%20Venmo (last visited Apr. 14, 2023).

[53] *PayPal Balance Terms and Conditions*, PAYPAL, https://www.paypal.com/us/legalhub/pp-balance-tnc?locale.x=en_US#:~:text=If%20your%20Balance%20Account%20is%20not%20eligible%20for%20FDIC%20pass,with%20state%20money%20transmitter%20laws (last visited Apr. 14, 2023).