

# PAYTECHS OF CANADA

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September 29, 2020

## New Membership Model for Payments Canada

**Leah:**

Thank you for the opportunity to be part of Minister of Finance's FinPay Committee and having the ability to engage with many of Canada's business leaders and Finance staff on the important issues facing the payments system. On behalf of the PayTechs of Canada association, we are very pleased to participate. I am now writing to you in response to your August 24th email, "FinPay Update". At this time, I would like to submit the following comments to the draft FinPay paper, "Considerations for a new membership model for Payments Canada" dated February 2020.

As you are aware, PayTechs of Canada was established in the spring of 2019 with the primary purpose of establishing a credible voice to represent the rapidly emerging Paytech sector of our economy. While the efforts of Payments Canada to survey the broader ecosystem and the diversity its Stakeholder Advisory Council provide a lens into the rapidly expanding and emerging markets that is PayTech, it cannot easily nor accurately reflect the diversity of views and issues of the more than 1,000 paytechs on Canada.

PayTechs of Canada, as a not-for-profit association, provides a harmonized voice for Canadian paytech firms working to improve payments systems and creates opportunities to provide a real value proposition for the benefit of all Canadians, businesses and government who rely on the payments system daily. As seen in a many international jurisdictions, the profile and prominence of paytechs are growing and their positive impacts are being widely recognized.

For paytech firms, having access to the national payments system is critical to their success but more importantly, for bringing about new products, services and processes into the payments system that reduce or eliminate many of the traditional or embedded frictions. With an appropriate regulatory framework for these new entrants, the financial services market will become much more competitive and the benefits from that competition, in terms of new and more efficient services and lower prices, will result. In the end, users of the payments system benefit and at a macro level, Canada's global competitiveness can only improve.

For your consideration, I wish to submit the following general comments:

- Establishing fair and reasonable access to Canada's national payments system, and satellite payments systems (e.g., Interac), is critical to the sustainability of the emerging market for PayTechs;
- The rapid introduction of legislation and regulation to support the expanding roles and responsibilities of paytech firms is equally as critical. Delays in the underlying legal framework only create further obstacles for new entrants, as incumbents aggressively recruit new subscribers well ahead of any authorized paytech firms. Past experience clearly shows there is a stickiness to transferring accounts

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to another institution, validating a significant “first-mover advantage”. Further delays serve only to disadvantage payments service providers and the financial services sector.

- When considering a new category of membership within Payments Canada, this must not be viewed in isolation. Membership, system(s) access (direct/indirect), levels of participation (e.g., data capture, exchange, origination of payment, clearing and settlement) and the implications of the current governance structure must be carefully considered and in unison. At any point, further barriers or obstacles could be established (i.e., intentionally or not) that could undermine the achievement of the public policy objectives to promote competition (i.e., ensuring contestable markets) that result in enhanced welfare for all users. Clear statements of policy direction and the articulation of guiding principles are necessary to guide this effort.
- Costs of participation in the national payments system are also a consideration. Clearly, no one would support paytech firms free-riding on the existing system, but similarly, it is reasonable to expect that the cost to participate in the system should not be a significant hurdle to participation. As a nascent industry, paytechs look to gain a toe-hold in the financial services market so that it can further develop and expand offerings to bring about greater payment-related efficiencies to Canadians.
- Based on the Membership proposal to date, expanded authorities or functionalities appear absent. As suggested earlier, membership must go hand in hand with added roles and responsibilities as membership will come at a cost (i.e., yet to be determined). PayTechs of Canada cannot support the creation of a “social” membership category in Payments Canada. PayTechs are seeking to become equal partners in the payments system, with comparable roles and responsibilities and the relevant costs to be borne by them should be directly related to the authorities provided and the functions undertaken by each.

## Questions posed:

Q1: Should additional membership requirements be considered for associate members independent of system-based access requirements?

- The membership responsibilities/obligations of current members are quite extensive so little must change to support the emerging players. Consideration should be given to a requirement that the applicant be registered and be in compliance with RPOF, once it is passed;

Q2: Would the access requirements to individual systems need to differ between associate members and regular members? If so, why and in what area?

- No, access should be made subject to fulfilling the future market conduct/prudential requirements established under the RPOF, if any. The Government of Canada regulations should address any system-related risks of concern and the direct oversight arising from the RPOF should be more than sufficient to address these concerns;

Q3: Should tiering of associate member rights and responsibilities be explored based on the roles they could perform to different payment systems?

- Articulating the range of roles/responsibilities is paramount for any analysis or discussion about the draft framework. As a member, they should be responsible and liable for their actions and the payment (related) functions/services they make available. In the absence of understanding the roles and responsibilities for PSPs, it would be inappropriate to proffer a response at this time.

Q4: Should Associate members be liable for extraordinary expenses?

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- It is unclear what these expenses would include. PSPs should be held liable for the functions and services that it directly provides. Any additional expenses would need a clear rationale and must not act as a barrier to entry that would otherwise prevent PSPs from access to the national payments system;

Q5: Should the liability model for associate members reflect the extent of their participation in Payments Canada's systems and their degree of influence over payments Canada's governance?

- The liability model should reflect the functions and services the members makes available by leveraging the systems of Payments Canada. In other words, the liability of all members should be proportional to the size and extent of business leveraging Payments Canada's infrastructure. The governance model should have no impact on a specific class of member, since it acts on behalf of the entire organization. Considerable efforts were expended in years past to present a governance model that was completely independent thereby eliminating the potential for bias and activities that were self-serving to any particular group or class of member. As the payments system is increasingly a heterogeneous group of firms, as opposed to pre-1980 where it was bank-only, the directions and decisions of the Board must reflect the broader interests of the entire membership and in the best interests of the association. Clearly, a representative board is challenged to do just that and park their proprietary interests at the door.

Q6: What other considerations should be assessed in determining associate members' liability framework?

- These should be the same considerations that exist for any member of the association. Liability arises from the actions of a member that may be contrary to the rules of the association, all of which should broadly apply to all members.

Q7: Does the current compliance framework, including compliance panels and suspension powers of the President remain appropriate for associate members?

- Yes, for the most part. The panel must however, broadly represent the membership, including any associate membership. Appeals of decisions must be within 30 days and to the Board of Directors. Given the significant representation of incumbent financial institutions on the Board, the appeal process should be limited to the independent members of the Board only.

Q8: Should additional tools be added to Payments Canada's compliance framework to ensure safety and soundness of the core payments systems?

- No, there are ample protections to safeguard the public policy objectives for Payments Canada via the majority independent governance model; the Ministerial review and disapproval process; the on-going engagement with the Bank and Finance pursuant to their MOUs with Payments Canada; Ministerial directive powers; and various consultative processes. Adding further tools will only serve to invite further delays to the achievement of the legislative mandate.

Q9: Should the funding model for associate members be based on their access and governance rights in Payments Canada?

- Funding should be based on a value proposition to the PSPs. Access without participation rights and authorities is effectively without any value.
- In terms of the governance model, PayTechs of Canada continue to support a fully independent board model as it introduces the least amount of bias from system participants

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and provides a greater amount of confidence that board directors will all honour their fiduciary responsibility and make decisions that are truly in the best interests of the association and not of their respective institution. The Board guides the overall payments organization in the attainment of its legislated mandate and as such, this role should not impact the allocation of dues. In fact, it would be prudent for the Board to clearly acknowledge and state that dues are a function of members' usage and should therefore be fair and equitable across the organization.

Q10: What factors should be considered to assess whether associate members should pay the same system-specific transaction and service fees as regular members?

- The are 2 key factors in this decision: 1) rate of usage of the various system/services provided by Payments Canada; and 2) ability to pay. As a nascent industry that has been denied access to the payments system for years, they have not been able to develop the services and customer base as the incumbent financial institutions. Recognizing the fragility of their current situation and the government's desire to aide in the establishment of a sound and thriving paytech sector, consideration may well be appropriate for this new class of member to received special treatment in the short run and receive a reduced dues assessment for a period of time (e.g., 5 years).

Q11: What factors should Payments Canada consider to determine what common services are of equal benefit to regular and associate members?

- It is unlikely that most if not all of Payments Canada's services provide equal benefit to PSPs and deposit-taking institutions under todays legal framework. The key to this assessment would be a matter of dependency. If PSPs continue to be dependent upon the larger institutions for services such as clearing, settlement, connection service providers, payment authorization/authentications, it would be unlikely that an argument could be developed to suggest an equal level of benefit results. In any tiering system like today's ACSS or LVTS, the indirect participant is always placed at a disadvantage both in terms of cost and process timing. The agency risk that exists between the direct and indirect participant is significant and the practical requirements currently in place perpetuates the class disadvantage and only harms the level of competition and competitive benefits in this market.

Q12: Should representatives from associate members be eligible to sit on the Board? Under what conditions?

- If you continue to support the existing model, then yes. However, PayTechs of Canada cannot support a decision-making "governance" model that continues to grant market power to the large incumbents and a mechanism to exercise this power through the operation of a Board of Directors. We would fully support a move to a completely independent Board of Directors, supported by member and stakeholder committees and under the direct scrutiny of the Minister of Finance and Governor of the Bank of Canada.
- The exercise of market power, in whatever form, is counterproductive to the smooth operations of the payments system and our desire to foster innovation and maintain a leadership role in payments, globally,

Q13: If so, should associate members be eligible for a prescribed number of seats on the Board? Should there be any restrictions while the number of entities seeking associate membership and the future extent of their participation on specific Payments Canada systems remains unknown?

- Further to the above comment, it is absolutely paramount that independent directors, excluding Payments Canada's CEO, must, as a minimum have the majority of votes.

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- Since the ultimate size and distribution of the Board is subject for extensive debate, PayTechs of Canada reserve comment on this question.
- During the last round of governance discussions, it was long held that the preferred model was a small but independent Board supported by expert committees and effective consultations. A move back to a representative board is a regressive step and inconsistent with industry best practices.

Q14: Should representation on the Board for all members vary based on other criteria such as system participation, similar to current seats reserved for members with settlement accounts at the Bank of Canada?

- The establishment and maintenance of a “representative” board is not consistent with the policy direction that had been developed since 2000. The payments system, as a critical essential facility, must operate in the broad public interest which is virtually impossible, as evidenced by the many “bank-friendly” decisions of Payments Canada over the past 25 years. The move to a majority independent Board facilitated research and policy development with the public interest in mind but the ability for the company to execute on these decisions has been adversely impacted by the actions of the large incumbents. An independent Board with the authority to effectively advance their decisions (e.g., direct proprietary system changes be completed within a specified timeframe) would be a welcomed departure from the current situation and expedite innovations. The challenge is that Board-approved rule changes often require member actions/improvements to their proprietary systems. Members can and do stall developments simply by delaying internal system changes.

Q15: Should associate member be entitled to participate in votes?

- Members of Payments Canada have a range of voting rights from those on the Board to those that participate at the Annual General Meeting. We must be clear on what voting rights are under consideration. As a general comment, all members should have the right to vote on matters impacting the corporation. The question becomes to what extent and are all members equal (1 member – 1 vote) comparable with that at the Board of Directors.

Q16: If so, should associate members be given a vote of equal weight to regular members? What considerations should be taken into account for matters that associate members may be eligible to vote on?

- The critical decision is “what decisions will be put to a member vote?” Shifting the decision-making power of the Board to members and then allocating a disproportionate number of votes to one class of members clearly undermines the direction of governance changes in Payments Canada over the past several years. The payments system is increasingly made up of diverse organizations, not just banks, and the collective intellectual power of this group is leading to real, positive and sustainable changes. Reverting control over key decisions back to the large incumbents will not serve the interests of Canadians nor the financial services marketplace.

Q17: Should associate members be eligible for representation on MAC?

- Yes, but PayTechs of Canada would prefer the establishment of a new committee, PAC, PayTechs Advisory Committee and whose structure and reporting requirements emulate that of the MAC. Moreover, like the SAC, the PAC would be provided consultative access to both the Bank of Canada and Finance Canada with the opportunity to meet annually with the Minister of Finance.

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Q18: Should non-member entities eligible for associate membership remain eligible for representation on the SAC?

- During a specified period of time (3 years), yes. Once the transition to Payments Canada's membership is complete and the governance processes to support the introduction of PSPs as members have matured, this will cease to exist.

Q19: Should there be a distinction in the rights and responsibilities between associate members seeking access to Payments Canada's systems and those not seeking access? In what ways should they differ?

- Those PSPs that refuse to seek membership in Payments Canada but wish to originate/deliver payment items directly into the system must be required to become a member. Alternately, PSPs may continue to participate indirectly in the system, through the facilitates of an existing member and in which case, membership is not required. The authorities and functionalities sought by the PSP will dictate whether membership is necessary.

Q20: Should there be different rights and responsibilities for members with direct ownership affiliation with other members?

- No.