

International Emerging Payments Landscape and E-Commerce Facilitation: The Regulatory and Business Environments in Key Markets Abroad, Lessons Learned for the U.S. Market, Strategies for Ensuring Compliance with Evolving Global Regulations

Canadian Emerging Payments: Legal and Regulatory Developments and Mobile Payments in Haiti: The Canadian Connection



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Regulatory Developments



Previous Actions Taken by Government

- In 2009, two parliamentary committees held hearings on the credit and debit card systems in Canada.
 - From March to May 2009, the Senate Standing Committee on Banking, Trade and Commerce held hearings on the credit and debit card systems. In June 2009, it released the report, “Transparency, Balance and Choice: Canada’s Credit Card and Debit Card Systems”.
 - From May to November 2009, the House of Commons Standing Committee on Industry, Science & Technology held hearings on credit card interchange fees and the debit card system.
 - In September 2009, the Government promulgated new credit card regulations, the *Credit Business Practices Regulations* and regulations amending the existing Cost of Borrowing Regulations, that require issuers to provide increased disclosure for consumers, and to make changes to customer documentation and business practices.

Previous Actions Taken by Government

- In May 2010, the Minister released a final version of the *Code of Conduct for the Credit and Debit Card Industry in Canada*.
- Code is “voluntary” but it has been publicly adopted by all payment card networks
- The objective was to foster transparency, disclosure and choice for merchants regarding the acceptance of credit and debit cards.
- Under the Code, merchants must be provided with clear information regarding fees and rates, given advance notice of any new fees and fee increases, and given the right to cancel contracts without penalty should fees rise or new fees be introduced.
- Part of the Code came into effect in August 2010 and the remainder in May 2011. The Financial Consumer Agency of Canada (FCAC) is monitoring compliance of networks, issuers and acquirers with the Code.
- With the passage of the *Payment Card Networks Act* in July 2010, the Minister of Finance has the power to regulate the market conduct of card networks and their participants through the promulgation of regulations.

The Task Force for the Payments Systems Review

- The initiative was announced on June 18, 2010 by the Minister of Finance of Canada and the final report released in March, 2012.
- Mandate was to examine the Canadian payments system with the goal of articulating key recommendations to guide the future of payment systems in Canada
- The mandate included:
 - identifying public policy objectives in the operation and regulation of the payment system
 - identifying and assessing the regulatory and institutional structures best suited to achieve these public policy objectives
 - assessing and reporting on safety and soundness of the Canadian payments system
 - assessing the competitive landscape for current participants including identifying potential barriers for new entrants and mechanisms to improve the competitive landscape
 - examining innovation in the domestic payments system and reporting on the challenges and opportunities
 - reporting on whether consumers and merchants are well served by the current system

The Task Force Report: *Moving Canada into the Digital Age*

- Task Force Highly Critical of Current Payment System:
 - Lack of innovation: Canadians still rely on outdated methods of payment such as paper-based processing and cash and cheques.
 - Insufficient competition and too many barriers to entry: payment system is outdated because it is dominated by the major Canadian banks and other key institutions whose interests are best served by keeping at bay new entrants.
 - Unless Canada develops a modern digital payments system, Canadians will be unable to engage fully in the rapidly evolving digital economy of the 21st century, leading to a lower standard of living across the country and a loss in international competitiveness.
 - Other countries are outpacing Canada's transition to digital payments.
 - Transactions are less data-rich than they need to be.
 - Electronic payments are not instantaneous.
 - Too much reliance on paper and cheques.

The Task Force Report: *Moving Canada into the Digital Age (cont'd)*

- Government of Canada needs to take the lead in several critical areas:
 - A feature-rich electronic invoicing and payments system for businesses
 - Partner with private sector to create a state of the art mobile payments system for consumers
 - Propel the build of a secure digital identification and authentication regime
 - A governance structure to allow collaboration and innovation
- To implement these initiatives, the Task Force proposed that legislation be introduced to accomplish the following:
 - Define the payments industry as a bona fide and discrete industry
 - Creation of a public oversight body (“POB”)
 - POB would assess the level of risk, competition and innovation in the payments system, monitor how changes to the payment system are implemented and that it reflects the needs and wants of the public, provide guidance when industry cannot agree on a solution
 - Take action if private sector behaviour no longer consistent with public interest as determined by the legislation.
 - Oversight body to delegate its regulatory and policy-making functions to a self-governing organization (“SGO”) while retaining the right to ratify the strategies of the SGO and review its performance.
 - Reform the Canadian Payments Association
 - Reinvent the objects, governance, powers and business models

Response of the Minister of Finance

- Various initiatives announced:
 - Establish the Finance Canada Payments Consultative Committee (“FinPay”) to help the Government stay abreast of market developments and to contribute to policy development in support of an innovative and safe payments system.
 - Review the Code of Conduct for the Credit and Debit Card Industry in order to respond to the evolution of mobile payments; and
 - Take a “fresh look at how the Canadian payments system and its participants are governed to ensure con-tinued safety and soundness of the system, while spurring innovation and promoting consideration of user interest.”

Possible Outcomes of the Task Force Report

- Task Force favoured “light touch”, non-prescriptive regulation.
 - Collaboration by users (consumers and merchants) and suppliers in the development of codes of conduct and rules.
- Regulation of interchange unlikely.
- Amendment of the *Code of Conduct for the Credit and Debit Card Industry in Canada* to provide greater transparency to merchants and consumers.
- Principles-based legislation instead of prescriptive legislation.
- Regulation of the activity, not the actor.
- Further study.

Canadian Near-Field Mobile Payments Reference Model

- The Task Force asked Canadian financial institutions to develop mobile payment guidelines for various participants in the Canadian mobile commerce ecosystem.
- Canadian Bankers Association coordinated the development by Canadian banks and credit unions of a Canadian Near-Field Communications (“NFC”) Mobile Payments Reference Model. The first version was published on May 14, 2012. Reference model has been adopted by major banks and credit unions.
- Deals only with payment card credentials on a SIM card or embedded in the secure element in the smartphone
- Provides a detailed blueprint for how NFC mobile payments can be offered in Canada, how open mobile wallets will be and how consumer privacy will be assured, including guidelines around how information is exchanged among various parties to a transaction including financial institutions, payment card companies, telecommunications companies and merchants.
- Provides a framework for the interaction between the different ecosystem participants.
- Other participants may participate in the mobile payments market by building mobile wallet applications for consumers such as government issued identification, library cards, transit passes, and merchant loyalty cards.
- CIBC and Rogers Communications Inc. announced plans to launch a joint NFC mobile payments service in Canada. The service, due to launch "later this year", will enable consumers to store multiple Visa and MasterCard CIBC credit cards on a SIM-based secure element in a Rogers NFC phone and use them to make payments at any merchant equipped with a contactless POS terminal.

Canadian Near-Field Mobile Payments Reference Model

- Focus on software and interoperability of components:
 - NFC mobile devices will be able to operate with different POS systems.
 - different credential providers will be able to operate on various NFC devices.
 - Any NFC contactless reader compliant with specified ISO standards will be able to communicate with any NFC mobile device.
- Three types of mobile wallets described:
 - Proprietary or closed – only payment credentials from wallet provider.
 - Collective – only payment credentials issued by a member of the group may be used.
 - Open – payment credentials from multiple credential issuers can be used to make payments. Need agreements between credentials issuers and wallet providers.
 - To promote openness, no restriction on access permitted.
- Outlines the installation, use, maintenance and termination of payment and wallet applications – emphasizes sound contractual relationships.
- Loyalty program information can reside on SIM card.
- General principle- participants should have access only to minimum information required to perform its primary role and adopts PCI-DSS.

Litigation Developments



Competition Bureau Alleges Anti-Competitive Conduct by Visa and MasterCard

- Application brought by the Canadian Competition Bureau before the Competition Tribunal to strike down what it considers to be restrictive and anti-competitive rules (e.g. the “Honour All Cards” rule, rule prohibiting surcharging, and rule prohibiting merchants from encouraging consumers to consider lower-cost payment options such as cash or debit) that Visa and MasterCard impose on merchants who accept their credit cards.
- Bureau alleges that these rules have effectively eliminated competition between Visa and MasterCard for merchants' acceptance of their credit cards, resulting in increased costs to businesses and, ultimately, consumers.
- Visa and MasterCard's rules are being challenged under the price maintenance provisions of the *Competition Act (Canada)*. The Bureau launched its investigation in response to complaints by merchants and initiated a formal inquiry in April 2009. Hearings commenced in May, 2012 .
- Visa and MasterCard are vigorously defending these provisions during the upcoming Tribunal Hearing.
- Visa responded that: Visa’s no-surcharge and honour all cards protections preserve consumer choice at checkout and ensure cardholders are not unfairly penalized for using their preferred form of payment.

Competition Bureau Alleges Anti-Competitive Conduct by Visa and MasterCard (cont'd)

- “Merchants already have numerous options available to help manage their payment acceptance costs, while receiving all the benefits of electronic payments including faster checkout times, guaranteed payment, and enhanced record keeping. Further Visa's policies do not preclude retailers from offering incentives or discounts to consumers who pay with their preferred payment method.”*
- Previously, in 2008, Bureau announced it would not take enforcement action against financial institutions that simultaneously issued multiple credit card brands or acquired transactions for multiple credit card networks

*Visa Canada press release, May 8, 2012

Marcotte v. Bank of Montreal et al

- Class action case in which it was alleged that unauthorized/undisclosed conversion fees were charged to credit cardholders in connection with foreign currency transactions.
- Superior Court of Quebec (2009):
 - Failure to disclose the conversion fee considered by the court to be in violation of Quebec *Consumer Protection Act*.
 - Provincial consumer protection legislation applies to federally regulated banks in matters of credit and credit cards notwithstanding the exclusive federal jurisdiction over banking under Section 91(15) of the *Constitution Act*, 1867 and the doctrine of paramountcy.
 - Members of the class are entitled to the reimbursement of foreign currency conversion fees that were charged illegally and punitive damages totalling approximately \$200 million.
- Court of Appeal decision in August 2012 allowed in part the credit card issuers' appeal and reversed lower court decision on punitive damages and disclosure of the conversion fees as part of the credit rate. However, the judgments against the issuers for having failed to disclose the fees for a period of time was maintained as such failure was found to offend the Quebec CPA and the Bank Act.
- Judicial harmonization removed necessity to resort to constitutional resolution rules.
- Parties have until October 2, 2012 to appeal to Supreme Court of Canada.

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- Members of the class are entitled to the reimbursement of foreign currency conversion fees that were charged illegally and punitive damages totalling approximately \$200 million.
- Decision under appeal to Supreme Court of Canada.

Mobile Payments in Haiti: The Canadian Connection



Mobile Payments in Haiti: The Canadian Connection

- In November, 2010, Canada's Scotiabank, Caribbean telco Digicel and Latin American mobile banking and payments software firm, Yellow Pepper launched the Tcho Tcho mobile service in Haiti.
 - Only 10% of population had bank account in 2011*
 - 80% have access to a cellphone*
- Mobile wallet service (run by a network of 960 agents) enables Haitians to carry out cash withdrawals, deposits and P to P transfers via their mobile phones without needing traditional bank accounts.
 - 500,000 users, 960 agents
 - 6 million transactions processed in 2011
- Yellow Pepper supplies and manages the agent network, IT infrastructure and payments software for the service. Scotiabank is responsible for registering agents and ensuring compliance with Haitian financial regulations.
- Two types of accounts both of which function as stored value accounts. No cost for opening accounts; small transaction fees for cash-out, transfers and POS payments, etc.
- *Source: U.S. Agency for International Development, quoted in an article on "Mobile Payments in Haiti".

Mobile Payments in Haiti: The Canadian Connection (cont'd)

- Basic account has maximum account balance of HTG 4000 (\$100).
 - No requirement for identity documents when funds deposited at agent location
 - Users must provide ID when withdrawing more than the equivalent of HTG 4,000 (\$100) out of their basic account.
 - Max daily transaction limit: HTG 4,000 (\$100)
- Other type of account has a maximum account balance of \$250 and requires users to provide a national identity document (ID card, passport, or driver's license)
 - Max daily transaction limit: HTG20,000 (\$500)
 - Total monthly amount: HTG 60,000 (\$1500)
 - Max value per transaction: HTG 10,000 (\$250)
- These limits are in compliance with La Banque de la Republique d'Haiti's "Guidelines for Banking At Distance" regulatory framework established in 2010.
- Framework requires FI to take responsibility for mobile money services, including approval of and contracting with agents. Bank has total responsibility for all deposits, including maintaining adequate reserves.
- This is a pre-funded model, with good funds, no settlement risk, transaction completed in real time. Super agent deposits funds with bank, once cleared, Bank loads Super-Agents wallet, ensures electronic and cash liquidity.

Mobile Payments in Haiti: The Canadian Connection (cont'd)

- Agents are either super-agents or standard agents
- Super-agents provide e-money to agents, have relatively large start-up capital, must keep enough cash on hand to execute transactions for agents and Tcho Tcho Mobile clients
 - Their daily transaction limit is HTG 1million (\$25,000)
- Standard agents register and train new Tcho Tcho Mobile clients and perform cash-in and cash-out transactions
 - Their daily transaction limit is HTG 200,000 (\$5,000)

How the transaction works

1. The customer establishes a Tcho Tcho Mobile account through a standard agent; deposits money to the account via the agent.
2. Customer sends a text message to T-T Mobile that includes the dollar amount to be paid and the receiver's mobile phone number.
3. T-T Mobile sends a text message back to the customer confirming the transaction and requesting the customer's personal identification number (PIN) to authenticate the payment.
4. Customer texts the PIN to T-T Mobile, who then transfers the requested dollar amount to the receiver's account with the T-T Mobile.
5. T-T Mobile immediately notifies the receiver of the payment.
6. Receiver can then obtain physical payment at standard agent locations or can hold funds in his electronic wallet.

Mobile Payments in Haiti: The Canadian Connection (cont'd)

- Services:
 - Payroll and cash for work payment services to private businesses, NGO's and Haitian government.
 - Domestic P2P transfers, bill payments to registered billers, and airtime top-up for Digicel accounts at a discount.
 - Conditional cash transfer payments where NGO's or Haitian government disburse cash to social welfare recipients provided they meet certain criteria.
 - Digicel launched Tcho Tcho Mobile Service with Scotiabank but intends to widen the number of banks to include 5 Haitian banks in a multi-bank model
 - New services to be offered include international remittances, loan accounts and savings accounts, micro-insurance
 - Instead of SMS messaging, the Service uses a protocol Unstructured Supplementary Service Data (USSD) for wallet transactions which enables GSM-based cellphones to communicate in real time with service providers while SMS messaging is used for confirmations (receipts).

The Initial Report Card: Comparison with Physical Delivery of Cash*

“Where a strong banking infrastructure and credit card network exist, NGOs have delivered services using pre-paid and smart cards. In places without this infrastructure, mobile-based solutions have emerged as a preferred option.”

- **Faster**
 - Distributing and receiving cash and paper vouchers requires considerable time and human resources
- **Safer** Avoids risk of loss and theft particularly when transporting physical cash to remote locations
 - Cheaper, since it streamlines processes and decreases the costs of transportation, security, voucher purchase, and cash preparation
 - Increased financial inclusion as the MM ecosystem matures in Haiti and greater value-added services enter the market
 - Increased privacy
- **Not cheaper, initially**
 - But one-time costs associated with launch of a new product and nascent ecosystem will decrease as institutional knowledge builds within NGOs and beneficiaries become more accustomed to the use of MM.

*Source: *Plugging into Mobile Money Platforms: Early Experiences of NGOs in the Field*, January 2012 by Dalberg Global Development Advisors for the Bill and Melinda Gates Foundation

Issues

- Regulation – limits on amounts stored on e-wallet required customers to cash-out before new funds could be transferred to it.
- Agents and vendors are sometimes challenged by high spikes in activity around payment cycles and settlement process with agents and super-agents responsible for in liquidity issues at merchants.
- Incorporating Beneficiaries
 - ID Requirements
 - Mini-wallets have lower ID requirements
 - Poor understanding of nature of the wallet
 - Ability to purchase from only from specific vendors limits the beneficiaries' experience of the service
 - Requirement to cash-out before new transactions can be performed

QUESTIONS?

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