

September 29, 2017

**VIA EMAIL: [fin.legislativereview-examenlegislatif.fin@canada.ca](mailto:fin.legislativereview-examenlegislatif.fin@canada.ca)**

Director, Financial Institutions Division  
Financial Sector Policy Branch  
Department of Finance Canada  
James Michael Flaherty Building  
90 Elgin Street  
Ottawa ON K1A 0G5

**RE: Comments on *Potential Policy Measures to Support a Strong and Growing Economy: Positioning Canada's Financial Sector for the Future* (the "Paper")**

Dear Director:

These comments are submitted on behalf of PayPal Canada ("PayPal"), in response to the Department of Finance Canada's (the "Department") review of the financial sector framework. We thank the Department for the opportunity to participate in this important conversation.

PayPal believes that a well-functioning financial system is essential to achieving inclusive social and economic innovation. We look forward to working constructively with the Department, and other stakeholders, to ensure Canadians enjoy a safe, reliable and modern financial services ecosystem that is conducive to inclusive economic growth.

PayPal consents to the disclosure of these comments, subject to removal of any personal information and designated confidential information highlighted in yellow.

## **1. Executive Summary**

Founded in 1998, PayPal is a leading technology platform company that enables digital and mobile payments on behalf of more than 210 million consumers and merchants in more than 200 markets worldwide. We offer online and mobile merchant acquiring services, money transmission and the most popular digital wallet in Canada. In some markets, we also offer business and consumer credit products. Headquartered in Toronto, with offices in Vancouver, PayPal Canada was incorporated in 2006. We have more than 6.4 million customers, including more than 250,000 business customers in Canada.

In order to offer services to our customers in Canada, PayPal operates as part of the financial ecosystem, in conjunction with and in reliance on other industry players, including banks, payment card network operators and acquirers. This, of course, is true of all fintechs. PayPal operates in an open access manner: we are technology and platform agnostic with relationships with countless banks, payment systems, operating systems, and platforms.

PayPal is a proud partner to several technology incubators and accelerator programs across the country, including the BC Technology Industry Association, the MaRS financial technology cluster and Ryerson's DMZ, among others. We are also an active participant in a number of consultations and conversations on financial sector policy in Canada, including as a member of the Finance Canada Payments Consultative Committee and on the Payments Canada Stakeholder Advisory Committee.

## 2. Supporting a Competitive and Innovative Sector

As a company that places a premium on innovation, PayPal supports the Department's consideration of measures to enable increased innovation and competition in the financial sector. Canada ranks poorly on innovation and business spending on R&D.<sup>1</sup> Greater innovation in all areas of the economy, including in financial services, is necessary and warranted to boost productivity and growth.<sup>2</sup>

The Canadian banking sector is highly concentrated. With stable customer bases and little competition, the large incumbents have relatively weak incentives to innovate. In its final report in 2011, the Task Force for Payment System Review observed that Canada's payment system is controlled by the major banks and other key institutions, namely payment card networks whose interests are best served by keeping payment innovators at bay:

"Canadians continue to use an outdated payments system not necessarily because they prefer it, but because no viable alternative has been priced and promoted in a way that makes it attractive to use. Canada's system has simply not evolved in step with the wants and needs of its users, and this stagnation is standing between each one of us and a better standard of living. The reason for this stagnation? Our payments system is controlled by Canada's major banks and other key institutions. Their interests are best served by keeping at bay new entrants to the system, the very entrants who would bring the innovations that Canadians need."<sup>3</sup>

Yet, it is through collaboration with Canada's big banks that homegrown fintechs can achieve scale in a small, domestic market. Banks are the gateway to global growth for homegrown fintechs and successful collaboration between incumbents and newcomers is paramount. Collaboration can take many forms, including direct investment, referral arrangements, technology integrations, outsourcing and vendor relationships.

In the wake of the 2008, financial crisis, alternative lenders stepped in to fill a funding gap for small and medium-sized enterprises (SMEs). In the US, 25% of PayPal's Working Capital loans for SMEs went to the 3% of counties that lost ten or more banks since the 2008 crisis. Although Canada didn't experience bank closures like the US, this country has experienced similar funding gaps due to bank de-risking. In some cases, alternative lending platforms have stepped into the breach, often with referral arrangements from banks.

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<sup>1</sup> Dr. K. Lynch, P.C., FinTech Workshop, Competition Bureau of Canada, Ottawa, Canada. February 21, 2017, available at <http://www.competitionbureau.gc.ca/eic/site/cb-bc.nsf/eng/04210.html> (last visited on September 12, 2017), noting that Canada ranked 22nd in both innovation and business spending on R&D globally.

<sup>2</sup> Toronto Financial Services Alliance, *Seizing the Opportunity: Building the Toronto Region into a Global Fintech Leader*, available at <http://tfsa.ca/storage/reports/BuildingTheTorontoRegionIntoAGlobalFintechLeader.pdf> (last accessed September 16, 2017), noting that [although it is the undeniable financial capital of Canada], Toronto ranks in the middle of the pack in fintech ecosystems, globally, alongside Hong Kong and Berlin. Toronto lacks the maturity and experience of Silicon Valley, the highly attractive investment climate of New York and the established government support of the United Kingdom and Singapore.

<sup>3</sup> Task Force for the Payment System Review, *Moving Canada Into the Digital Age*, 4 (December 2011), available at [http://paymentsystemreview.ca/wp-content/themes/psr-esp-hub/documents/rf\\_eng.pdf](http://paymentsystemreview.ca/wp-content/themes/psr-esp-hub/documents/rf_eng.pdf) (last visited on June 19, 2015) [Digital Age].

PayPal supports measures to provide federally regulated financial institutions with additional flexibility to make investments in fintechs and the corresponding authority to make referrals. SMEs are the engine of our economy and can be particularly valuable in growing export markets. PayPal strongly believes that any step we can take to encourage innovation and competition in financial services is a step in the right direction towards inclusive innovation and commerce for SMEs and all Canadians.

#### Improving Regulatory Transparency and Coordination

PayPal supports the Department's commitment to working with provincial and territorial regulatory authorities to better coordinate and share information. Although PayPal is a sophisticated global fintech, with large dedicated legal and compliance teams, most Canadian fintechs are smaller firms with few resources.

At this critical juncture in discussions on regulations that will directly apply to fintechs or indirectly impact them, PayPal feels that it is incumbent upon the Department to do more to ensure that a diverse and representative group of domestic fintechs are informed and represented at the tables where policy discussions are taking place. PayPal agrees with the Department that these efforts will improve federal regulatory transparency and better position fintechs to grow and succeed.

#### Streamlining the Bank Entry and Exit Framework

The Department indicated it is seeking views on whether to undertake a series of targeted refinements to streamline and promote a smooth entry and exit process.

Similarly, we have heard stories of other fintechs having great difficulty obtaining banking services in Canada. As much as banks are the gateway for homegrown fintechs to scale and grow globally, they remain the gatekeepers to the Canadian financial services market. Due to high concentration of incumbents, it doesn't take many 'no's to effectively shut a newcomer out of the market.

PayPal believes this behaviour is anti-competitive and could be addressed through the adoption of basic business banking requirements, similar to what currently exists for consumers. Banks should be required to offer basic business banking to all qualified businesses. The requirements to determine who can qualify should be set by the Department, as a matter of public policy.

### **3. Positioning a Competitive and Innovative Sector to Support Long-Term Economic Growth**

The Department seeks views on how best to ensure that the financial sector supports long-term economic growth, while balancing the need for a well-functioning and stable sector.

Through disruption of existing business models and technology, fintech has the ability to deliver real benefits to consumers and businesses, particularly to SMEs. These potential benefits include increased choice, greater efficiencies, operational resilience, lower costs and better customer experiences, including increased transparency in relationships.

In order to realize these benefits, the Department should consider steps to ensure that disruption can and will occur, both inside and outside incumbent financial institutions. It is less important which entity

or technology disrupts, but rather that financial services can be disrupted by anyone with a better idea of how to provide those services in a manner which is safe, secure and reliable.

For incumbents, this means taking steps to provide additional flexibility to collaborate with fintechs and corresponding requirements for open banking (explained in more detail below) and the provision of basic business banking, as discussed above.

For fintechs, this means ensuring that the regulatory framework is appropriate and balanced. Wherever possible, regulations should be principles-based and not duplicative. Further, regulations should be focused on addressing appropriate risks.

Today, the regulatory framework for financial services in Canada, both for incumbents and fintechs, is complex and fragmented, with insufficient cooperation between levels of government and regulators even at the same level of government. PayPal respectfully submits that the Department should consider how it can rationalize the cumulative burden of regulation and facilitate reductions. The Department should also consider how it can facilitate increased cooperation and coordination across government and between governments.

#### **4. Examining the Merits of Open Banking**

Financial technology continues to make massive strides in helping consumers, businesses and governments better interact with financial services. A major factor in development and adoption of these technologies is access to and permission to use consumer data, often referred to interchangeably as “open access”, “open data” or “open banking”.

Open banking can take many forms. It enables consumers and small business to share their data securely with other banks and with third parties, to manage their accounts with multiple providers through a single website or mobile app, to take greater control of their money, and to more intelligently shop for financial products and services on their own terms. Open banking is fundamentally a more efficient, lower cost and more consumer-friendly model for banking.

In 2015, the European Parliament adopted the Revised European Payment Services Directive (“PSD2”). Beginning in 2018, PSD2 requires European financial institutions to allow authorized third-party service providers access to customer account information and initiate payments on a customer’s behalf with explicit consent. PSD2 represents the first major regulatory push for open banking.

Despite the importance of PSD2, many questions remain about how to achieve effective open banking, including in this country. Security of customer data should and the adoption of interoperability standards should be paramount. Fintechs that have a demonstrated track record of success with security and the ability to work with other stakeholders will be ideal partners for piloting and building out data access platforms.<sup>4</sup> Ultimately, the success of open banking will come down to customer trust. If customers don’t trust that fintechs are safe, secure and reliable, then no regulation to permit open banking will suffice. Customer trust will foster adoption of open banking models and spur future innovation.

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<sup>4</sup> PayPal is consistently ranked among top in consumer trust and security by Javelin, Forrester, & comScore. PayPal was a pioneer in beginning to tokenize data and has more than 1 billion tokenized financial instruments on file.

However, if the Department does not support open banking in Canada, banks will never voluntarily do so and innovation and competition will suffer. The lack of incentive for large banks in Canada to innovate is discussed elsewhere in these comments. In a 2016 report, the UK's Competition and Markets Authority ("CMA") concluded that established banks don't have to compete hard enough for their customer's business, while smaller and newer banks find it difficult to grow.<sup>5</sup> The CMA found that many people are paying more than they should be for financial services and not benefitting from innovation. To address this problem, the CMA is implementing wide-reaching reforms in the UK, including by recognizing non-banks as legitimate players in the marketplace and requiring UK banks to implement open banking by early 2018.

PayPal respectfully recommends that the Department support open banking in the Canadian financial services industry and work with the private sector to develop clear standards for security and interoperability.

## **5. Closing**

PayPal appreciates the opportunity to address the important issues raised in the Paper and look forward to working constructively with the Department and other stakeholders as this conversation progresses.

As a global payments innovator, operating in more than 200 markets around the world, PayPal has expertise in navigating the complex international regulatory framework. We bring a unique perspective on the payments industry and feel this is particularly valuable when charting a course in unknown territory. If the Department has questions or would like to discuss the topics addressed in these comments or others, please do not hesitate to contact us.

Sincerely,

PayPal Canada

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<sup>5</sup> Competition and Markets Authority, "Making Banks Work Harder For You" (August 9, 2016), available at [http://www.agefi.fr/sites/agefi.fr/files/fichiers/2016/08/cma\\_overview-of-the-banking-retailmarket\\_9\\_aout.pdf](http://www.agefi.fr/sites/agefi.fr/files/fichiers/2016/08/cma_overview-of-the-banking-retailmarket_9_aout.pdf) (last accessed on September 21, 2017).