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Via Email

Financial Systems Division
Financial Sector Policy Branch
Department of Finance Canada
90 Elgin Street
Ottawa ON K1A 0G5
Email: fin.payments-paiements.fin@canada.ca

Re: Consultation on the Review of the Canadian Payments Act (the “Consultation”)

Ladies and Gentlemen:

Payments Canada have requested comments and information to assist it in considering how best to adapt Payments Canada’s membership structure to ensure that access to its payment systems reflect developments in the payments market while ensuring that ongoing policy objectives are achieved. TransferWise appreciates the opportunity to comment on the Consultation, and to share its experience as the first direct non-bank member of the UK Faster Payment Service, and the first non-bank to hold settlement accounts at the Bank of England, and its strong belief that payments systems should be open to regulated non-banks.

Background

TransferWise is a financial technology company that was created in 2011 by Taavet Hinrikus, the first employee of Skype, and Kristo Käärmann, an ex-Deloitte consultant, out of their personal frustration with high fees charged on international money transfers. Since that time, TransferWise has raised more than \$397 million from investors such as Andreessen Horowitz, Sir Richard Branson, and Max Levchin, the co-founder of PayPal.

TransferWise addresses the challenges and costs associated with international money transfer — specifically the lack of transparency regarding fees and the calculation of foreign exchange rates — as well as the reliance on outmoded systems and technology. In response to these issues, TransferWise operates a robust international money transfer and stored value product that offers a fair, mid-market exchange rate, sources onshore liquidity when possible, provides a

straightforward and transparent fee structure, uses modern technology, maintains sound customer service practices, and carefully manages liquidity, compliance and other risks.

Each month, the TransferWise group handles over \$3 billion CAD equivalent in transaction volume for over 3 million customers worldwide, with approximately \$10 million in monthly CAD volume alone. More importantly, TransferWise estimates that its customers save over \$80 million CAD equivalent worldwide every month by using its platform over other providers. TransferWise has over 1000 employees and nine offices, with its head office in London. In Canada, TransferWise operates as a Money Services Business (MSB) and is registered with the Financial Transactions and Reports Analysis Centre of Canada (FINTRAC) and licensed by the Autorité des Marchés Financiers (AMF). In addition, TransferWise maintains appropriate licenses and/or is regulated in many of the other countries where it operates.¹

General Comments

TransferWise agrees that payment systems are essential to support economic activity and therefore strongly supports the Payments Canada initiative to ensure that systems are fast, secure, reliable, and flexible while fostering innovation and fair access. For some time, the international regulatory community has called for access to payment systems to be “open and risk-based”, which is consistent with the CPMI-IOSCO’s *Principles for Financial Market Infrastructures* (2013) (the “PFMIs”).² For this reason, TransferWise fully supports the premise that Payments Canada’s membership structure should ensure that access to payment systems reflects developments in the payments market. Notable developments include:

- Consumers’ expectations for payments experiences are changing – they expect inexpensive fees and modern technology, including the ability to use their mobile and other devices with speed and 24-hour convenience, and businesses have similar expectations as well as automated back-office operations, enabling the elimination of paper-based payment items and manual reconciliation. Additionally, users of all types expect access to their own account information through APIs.
- Fintech companies are attractive to consumers and business and are therefore growing, since they offer efficient solutions unburdened by legacy technology, and focus on

¹ In the US, TransferWise Inc. is registered with FinCEN and holds money transmitter licenses in nearly all of the states. TransferWise Ltd is registered with the Financial Conduct Authority (FCA) in the UK and with the Australian Securities and Investments Commission (ASIC), and is registered with the Financial Intelligence Unit (AUSTRAC) as a money remitter in Australia. In Hong Kong, TransferWise is registered with the Customs and Excise Department of Hong Kong and is licensed as a Money Service Operator. In Japan, it is registered by the Kanto Local Financial Bureau and licensed as a Funds Transfer Service Provider. In New Zealand, TransferWise is registered by the Department for Internal Affairs (DIA). In Singapore, TransferWise is regulated as a remittance business by The Monetary Authority of Singapore (MAS).

² See PFMI, Principle 18, Key Consideration 2 (“Subject to maintaining acceptable risk control standards, a [payment system, including generally those operated by central banks] should endeavour to set requirements that have the least-restrictive impact on access that circumstances permit.”).

improving convenience and usability and reducing cost. Positive changes in the payments space attributable Fintech companies were acknowledged by Payments Canada in its Consultation on A New Retail Payments Oversight Framework (2017) (the “**Proposed PSP Oversight Framework**”), and for cross-border payment service providers (“**PSPs**”) specifically, the BIS has recently recognizes that “in the payments and cross-border remittance businesses...the potential for [Fintech] firms to expand their cross-border operations is high.”³

In response to these developments, payment systems in many jurisdictions are modernizing and evolving their membership, and TransferWise has been part of several important initiates in this regard, including the rise of cross-border payments in the Single European Payment Area, the launch of the Australian Payments Network’s New Payments Platform to enable faster payments, the US Faster Payments Task Force, and the Bank of England’s project to modernized and open up its core systems, an effort by regulators and the government to “encourage competition in the UK’s financial sector.”⁴ The latter culminated in TransferWise, in April 2018, becoming the first non-bank direct member of the UK Faster Payment Service (FPS). To facilitate settlement in central bank funds, TransferWise also holds an RTGS account at the Bank of England.

Through our experience with these initiatives, TransferWise has found that open access to payment systems is extremely important for the following reasons:

1) It fosters competition

When firms face excessive barriers to entering a market, competition stagnates, prices remain high and innovation remains low. In many countries, banks are subsidized and insulated from competition, and exclusive access to payment systems is one of the ways competitors find themselves on unequal footing. In addition, bank often own the payments systems, in accordance with laws, regulatory policy and payment system rules, which further allows banks to crystalize rules that restrict access. In practice, banks are also often asked to both facilitate indirect access to payment systems, for a fee, and at the same time compete with those challenger payment systems, creating further conflict and undue control by the traditional financial services sector. This is inefficient and should be addressed through additional avenues for access.

2) It lowers costs for end users

Customers may be frustrated with certain aspects of traditional financial services, such as unfavorable foreign exchange rates, bureaucracy, or legacy technology, and therefore use a PSP

³ Basel Committee on Banking Supervision, *Consultative Document, Sound Practices: Implications of fintech developments for banks and bank supervisors* (August 2017) Page 6, Observation 6.

⁴ Nicholas Magew, *TransferWise becomes first non-bank to join BoE payment system*, Financial Times (April 18, 2018).

⁵ TransferWise, had, prior to 2018, had indirect access to the Faster Payment Service via Raphael’s Bank.

or other Fintech company, or they may use a Fintech company that provides services not offered by banks. However, when Fintech companies' transactions are settled through an intermediary, transaction costs increase for end users. For example, when TransferWise gained access to the FPS, the prices for transfers with a GBP leg decreased, and for that and other reasons, Transferwise was able to reduce fees for certain transactions by 20%.

3) It speeds up payments for end users

Indirect members of payment systems often have arbitrary cut-off times due to their intermediary that do not reflect the opening and closing times of the payment system, slowing down transfers. Having direct access to payments systems, and avoiding intermediaries, then tends to speed up payments, and since new payment systems are focused on near-instant receipt of funds, consumers expect fast payments. Direct access also gives the direct member fulsome oversight over its own transfer flows, so that if there is a problem with a transfer, it can be resolved as quickly as possible for the end user, which enables trust. In this way, direct access supports the principle of efficiency.

4) It reduces systematic risk

Banks' size and interconnectedness can contribute to systemic risk, and Fintech players without access to payment systems use banks to send payments, further concentrating this risk, as it is often the case that only a few banks host all of the indirect Fintech participants. It is well understood and stated in the PFMI, that final settlement of obligations in a payment system should be in central bank money where practical and available, because it is safer and less risky. *See PFMI, Principle 9.*⁶ Thus, direct access for Fintech's fosters safety and soundness for their customer's settlement funds by avoiding bank credit and systemic risk and allowing for settlement in central bank funds.

5) It reduces operational risk and overhead

When a Fintech company uses an intermediary, it takes on the operational risks of the intermediary as well as its own. Fintech companies would prefer not to take on this extra layer of operational risk and often have little power to influence their intermediary. In addition, Fintech companies would prefer to avoid the need to pass customer data to an intermediary.

6) Direct access gives the payment system the ability to perform more comprehensive risk oversight

When a fintech company is able to meet risk-related standards to join a payment system as a direct member, it will be contractually obliged to comply with the system's rules, standards, participate in loss allocations, and meet other requirements, and both the payment system and the

⁶ PFMI, Principle 3.9.3. "Central banks have the lowest credit risk and are the source of liquidity with regard to their currency of issue. Indeed, one of the fundamental purposes of central banks is to provide a safe and liquid settlement asset."

member can communicate directly information about incidents and risks, enhancing the risk outlook of both parties.

Specific Comments

Section 3: Payments Canada Governance

- 1. Have the 2015 changes to Payments Canada's governance been successful in better enabling the organization to achieve its public policy mandate to promote the efficiency, safety, and soundness of its systems while taking into account the interests of users?***

Yes. For the reasons above, TransferWise supports open access to payment systems and it follows, then, that TransferWise favors governance that will facilitate that principle, including a board that is free from conflict and is committed and incentivized to act in accordance with what is best for end users, efficiency and competition, and safety and soundness. TransferWise believes that independent directors are key to ensuring that incumbent banks do not capture the system, competition flourishes and that management is forward thinking, while maintaining a culture of safety and compliance with the PFMIs. TransferWise also supports the “one member one vote” framework, as it allows smaller players to have influence over the system. TransferWise further agrees that plans and financial statements should be provided to the public to ensure alignment and fair access to information.

- 2. Are there aspects of Payments Canada's governance structure that could be improved to better allow Payments Canada to carry out its mandate and serve its public policy objectives?***

As described in the response to question 4.1(3) below, end user needs should be further embedded into the rules of the system, if there should be a requirement for all payment system matters and changes to have a clear and documented end user impact assessment.

Section 4.1: Membership RTR

- 1. Should the Government create an associate membership class to facilitate access to the RTR? Should alternate approaches be considered?***

Under section 4(2) of the Canadian Payments Act (the “**Act**”), credit union centrals, trust companies, loan companies, certain other deposit-taking institutions, life insurance companies, securities dealers, and money-market mutual funds that meet certain prescribed requirements are eligible to become a member institution in Payments Canada. Under the Act, any Payments

Canada member institution is then eligible to become a participant in a payment system if it maintains a settlement account at the Bank of Canada, and meets certain other requirements.

Associate membership as described in the Consultation, is “separate and distinct from members, with a separate set of rights and obligations, and subject to Payments Canada's compliance and enforcement standards.” Assuming there will be compliance and enforcement standards in the Proposed PSP Oversight Framework once promulgated, it is unclear from the Consultation why associate members should have a “separate set of rights and obligations” and what those will be. While the idea of additional membership classes is a welcome change, TransferWise, as discussed above, fully supports direct membership of non-banks able to satisfy risk-based standards, and it believes it should be clear that PSPs will be given the ability to obtain direct access. To further this objective, a clear, simple application procedure needs to be created, including the granting of a settlement account to eligible PSPs, and the system should avoid the creation of undue costs in connection (e.g., mandatory software purchases) to avoid raising barriers to entry. In Hong Kong, for example, a new payment system that is going live in September 2018, which already allows access to a type of non-bank PSP, is granting connection through a simple and secure API.

2. *Should registration and regulation under the proposed retail payments oversight framework be a pre-condition for associate membership?*

TransferWise supports the Proposed PSP Oversight Framework subject to its comments submitted on and dated October 17, 2017, and agrees that registration and regulation under the proposed retail payments oversight framework should be a pre-condition for membership. Mutual trust and confidence among members and Payments Canada is necessary for the smooth operation of the payment system, and well understood and uniform regulatory regimes and registration requirements will foster such trust. TransferWise, as a global business, also very much appreciates reliance on a well-organized and widely agreed international framework, such as the PFMI, on which the proposed framework is based. Although the PFMI go well beyond what is necessary for the management of a PSP, they provide good pillars to help ensure that regulation, and in turn membership requirements, are risk-based and not arbitrary or anti-competitive.

3. *How could Payments Canada's governance structure be adapted to allow for appropriate reflection of associate member views into Payments Canada's decision-making process? In what ways could this be designed?*

While advisory councils may be a good way to seek advice and counsel from underrepresented stakeholders, it is important that members or associate members settling through the system have the actual ability to influence system governance and oversight. In situations where there could be conflicts, it is also important that associate or new types of members have a voice so that system rules and pricing are fair. As was acknowledged in the 2015 governance amendments, it

is vital that board members do not have conflicts between representing their employers and representing other members, and that board members are appropriately incentivized to foster competition and safety. Currently, Payments Canada's board is comprised of thirteen (13) members – of the five member-directors, three (3) are large direct participants in Payments Canada's systems with settlement accounts at the Bank of Canada, while the remaining two directors are drawn from Payments Canada's remaining members. If instead, six (6) members were independent (including the independent chairperson), of the remainder, we would suggest that three (3) should be large direct participants and up to three should be (3) associate members or PSPs, plus the CEO of Payments Canada. In this way, power is balanced and there is a tiebreaker in each of the ranks.

Independent directors could also be called upon to better promote fairness and the interests of end users. In the UK, for example, the Payments Council charged each of the independent directors with a specific mandate/end user objective so that each of them could exercise a veto if any proposal or decision worked against the end-user objective. In this way, each director maintained a relationship and consulted with its particular group of end users and exercised vetoes when necessary. Additionally, issues like pricing should be left to the decision of independent board members. As smaller members are added, the split between common service dues and volumes-based pricing, for example, will become more important and should be fairly decided by those with independence. Finally, we would encourage as much transparency around corporate governance and planning as possible, and suggest that member and associate voting could be used (one vote each) for key changes to rules and systems.

Section 4.3: Membership Lynx and Systemically Important FMs

1. *What are your views on whether and how to broaden membership so that systems that are designated by the Bank of Canada as systemically important financial market infrastructures can directly access Lynx?*

It may make sense to include systemically important systems as members, but equally there is no reason to exclude non-systemically important PSPs from the entity types currently named in the Act. For the reasons discussed in the General Comments section, TransferWise advocates for a broad membership criteria that is risk based. Fintech companies, as they grow, should be able to undertake large value transfers and will need safe and inexpensive methods of doing so. Typical wire transfers, for example, cost consumers around \$45 dollars, and in the cross-border space, there is a possibility for Fintech companies to facilitate large value transactions, for example, and use local payments systems in order to avoid the cumbersome and inexpensive correspondent banking system. Thus, any barrier to entry should be risk-based, and it should not be assumed that the outlook for large value payments is not evolving.

* * *

Again, we appreciate the ability to provide our comments and support the effort of Payments Canada to recognize the impact of emerging payment companies on financial services. Please do not hesitate to contact us if you have any questions regarding this letter and if we can be of any assistance as you move forward.

Yours faithfully,



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