PAYMENTS SYSTEM REVIEW

DISCUSSION PAPER

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1. Introduction

The payments system is the combination of institutions, instruments and services that facilitates the transfer of monetary value between parties to a transaction. It is the infrastructure that makes it possible for a variety of payment instruments to be exchanged in the economy for goods, services and financial assets. A safe and efficient payments system is essential to the operation of a modern and sophisticated market economy.

Canadians enjoy the benefits of a highly reliable and efficient payments system. In fact, the system works so well that it is largely taken for granted. The efficiency with which cheques and other paper-based payment items are cleared and settled, together with a high level of confidence in the system, allows payees to, in most instances, receive immediate provisional credit when they deposit a payment item at their financial institution. This is the case even though final settlement may not take place for some time thereafter.

A notable development in recent years has been the growth of electronic forms of payment, which offer new levels of convenience to consumers, lower processing costs for institutions, and new opportunities to monitor payment activities and control risks. Canadians have embraced these new payment methods, including direct debits to cardholders' accounts, credit transfers for such things as payroll deposits and monthly bill payments, and a range of transactions initiated at automated banking machines (ABMs).

These developments have made participation in the payments system more attractive, and perhaps more feasible, for a larger number of players than was the case when the system was designed primarily to clear and settle cheques. Such changes have also served to elevate the role of the payments system in the day-to-day activities of end-users. Consumers of payments services (both individual and corporate), as well as retailers, recognize the growing importance of the payments system to them, and want to be sure that their interests are being considered.

Another feature of the changing environment has been the way in which competitive forces in the financial sector have intensified. This has been due, in part, to government policies aimed at promoting broader competition in the provision of financial services, including efforts to eliminate certain distinctions between the traditional four "pillars" and allowing closer links among them. Expressions of this policy include the removal, in 1987, of the restriction on bank ownership of securities subsidiaries, and the granting of broad cross-ownership powers to banks, trust and loan companies, insurance companies and credit union centrals under the 1992 revisions to the federal financial institutions legislation. To a lesser degree, these institutions have also been given powers to provide a broader range of financial services "in-house".

In addition to contributing to greater competition in the provision of individual services, these changes have increased the potential for economies of scope in the provision of a range of different financial services, and provided additional benefits to consumers through the convenience of one-stop shopping. These forces have also led to more direct competition among a broader range of institutions offering such services as deposits, mutual fund and other investments, and annuities. As a result, different types of financial institutions, which once provided different services corresponding to distinct customer needs, have become providers of

overlapping sets of financial services, often in direct competition with one another. In this competitive environment, access to the payments system has taken on increased strategic importance.

In June 1996, the government responded to this changing environment by launching a payments system review (see Box 1). The primary objectives of the review were to determine whether access to the payments system should be broadened in response to the changes described above, and whether modifications to the governance framework for the payments system were needed to ensure the system would continue to develop in a way that best serves the public interest.

Box 1: ***The Payments System Advisory Committee***

In June 1996, the government announced that the Department of Finance would conduct a review of the payments system with the assistance of an advisory committee.

The Payments System Advisory Committee was composed primarily of individuals drawn from outside government – including the financial services sector, the retail and consumer sectors and academia. The Committee was co-chaired by senior officials from the Department of Finance and the Bank of Canada, and included representatives from the Office of the Superintendent of Financial Institutions (OSFI) and the Canada Deposit Insurance Corporation (CDIC).

The Committee first examined the structure and operation of the payments system in Canada, then the public policy objectives relevant to the payments system and, finally, in the context of those policy objectives, the issues of payments system access and governance. A series of four analytical papers were prepared for the Committee's discussion:

(1) **The scope and elements of the payments system.** The first paper describes the evolution of the payments system in Canada and provides a detailed description of the instruments, services, and participants involved in the system today.

(2) **The public policy objectives for the payments system.** This paper identifies the key public policy objectives for the payments system and the relationships among them, and considers some general approaches to achieving them.

(3) **Access to the payments system.** This paper reviews the existing access conditions for various components of the payments system, and highlights some of the concerns of non-deposit-taking institutions over the nature of the existing access regime. Some general options for broader access are also presented.

(4) **The means of achieving the public policy objectives, or the governance of the payments system.** The last paper reviews the existing legislative and decision-making structure for the payments system, and examines some of the key issues associated with that structure. The roles of government and the private sector are explored, and some alternative regulatory and decision-making arrangements are considered.

Copies of these papers, including a short summary of the Committee's discussions, may be obtained by contacting the Department of Finance. They can also be found on the Finance Canada web site at **http://www.fin.gc.ca**, or on the Bank of Canada web site at **http://www.bank-banque-canada.ca**.

At the outset of the payments system review, the government indicated that the review process would function in parallel to the work of the Task Force on the Future of the Canadian Financial Services Sector and that, while payments issues were being examined separately because of their technical nature, it would be important that the Task Force be aware of the work of the review.

The four papers prepared for discussion by the Payments System Advisory Committee, along with the associated summaries of discussion, were provided to the Task Force during the course of the review and were also made publicly available. The purpose of the present paper is to draw to a close the Advisory Committee process, contribute to the public debate of payments issues, and provide the Task Force with the additional background and analysis needed to consider payments issues in the context of its broader vision for the financial sector.

The remainder of the paper is organized as follows. Section 2 provides a brief overview of the key public policy objectives identified for the payments system. Section 3 deals with the issue of payments system access. The existing access structure is reviewed and some general criteria for payments system participation are developed. Finally, Section 4 discusses the issue of payments system governance. Issues surrounding the broad governance framework are outlined, and a number of options for change to the existing structure of decision making within the Canadian Payments Association (CPA), and the payments system more generally, are presented.

2. The Public Policy Objectives

The payments system review identified three primary public policy objectives for the payments system: efficiency, safety and the consideration of consumer interests. In the context of payments system reform, some changes may advance one or more objectives without sacrificing others. However, in other cases, trade-offs may be encountered. In the presence of such trade-offs, achieving the objectives is not straightforward, and the goal must be to find and promote an appropriate balance among them. This balance will be the combination of objectives that is judged to best serve the public interest.

Efficiency

To promote an efficient payments system, market arrangements and regulatory structures should allow users' payments needs to be satisfied in a timely fashion, at the lowest possible cost to suppliers and at competitive prices in the market. Automation and the use of electronic payment methods may contribute significantly to the achievement of this objective. In this regard, service providers should have adequate incentives for innovation, and the market and regulatory structures should be flexible to allow the rapid adoption of new and emerging technologies.

The payments system and its participants should be responsive to users' needs and demands, and should promote product and service quality in areas such as speed and predictability of settlement, and convenience of access to, and use of, payments services.

Finally, both suppliers and users of payments services must have adequate access to information to make informed decisions in the market. Emphasis should be placed on promoting adequate disclosure of the terms and conditions associated with the use of payments products and services, and of potential differences in risks among them.

Safety

Safety in the payments system means that participants have both the incentives and capacity to identify and manage the risks to which they are exposed, and that the system is governed by a comprehensive and transparent legal framework and is robust in the face of adverse shocks. All of these factors help to contribute to certainty in the payments process and reduce the risk of costly disruptions. To promote public confidence in the payments system, risks must be kept sufficiently low in terms of the frequency of payment failures and the size of the associated losses.

Achieving these objectives goes beyond ensuring that payments system participants are financially sound, as payment failures may be caused not just by the failure of a system participant, but also by failures in the operational mechanisms that underpin the system. As a result, network operating systems and procedures must be well designed and reliable.

Protecting the security of payment networks is also of paramount importance. It is incumbent on the individuals and organizations that provide payments services to develop systems that are secure and reliable, and to be able to detect and contain any security violations. As the payments landscape continues to evolve, and as old payment methods are replaced by new and increasingly electronic ones, security issues must be afforded ample consideration in order for the system's users and participants to reap the full benefits that technology may bring.

Finally, the system should embody appropriate risk controls and risk-sharing mechanisms to ensure that problems may be easily contained, and are not spread to other participants in the system, to other systems, and beyond the payments system itself to other aspects of the financial sector and the broader economy.

Consumer Interests

While the consumers of payments services clearly benefit from the achievement of an efficient and safe payments system, they also have a number of more specific interests. Of particular concern are the protection of personal information and the assurance of access to at least a basic set of payments services for all consumers.

Advances in information processing technology have made it increasingly easy to collect and analyze a wide array of personal information. Financial institutions and other service providers may find it increasingly attractive to use the data on individuals and their purchasing habits generated through the operation of the payments system to more effectively target their marketing efforts. This is not inherently a bad practice – it allows for a more efficient use of information and may have benefits for both institutions and their customers. The institutions may gain increased business by targeting services specifically at customers who may find them most attractive, and the customers themselves can benefit from having products and services they desire brought to their attention. However, there is also a clear threat to consumer privacy if information is collected and used without the knowledge or consent of the customer. It must be recognized, however, that this is not solely a payments system issue but is rather of general concern for consumers in all of their financial dealings.

As the payments landscape continues to evolve, and as cashless transactions become more and more the norm, access to payment services for certain individuals – for example, low-income consumers – is becoming an issue of greater significance. Most non-cash payments involve transferring balances between deposit or quasi-deposit accounts at financial institutions. Thus, limitations on access to these accounts may constrain the range of payment options available to these individuals. In addition, the shift toward more electronic payment methods may also require consumers to possess increasing levels of financial and technological sophistication. As this evolution continues to take hold, the government must be cognizant of the need for all consumers to have access to a basic set of payment options, regardless of their financial means or technical sophistication.

3. Access to the Payments System

Access to the payments system refers broadly to the ability to participate in various elements of the provision of payment services (see Box 2 for a review of the existing rules governing access to the payments system in Canada). This participation may be at any stage, including the initial provision of payment instruments and collection of payment information, the messaging services involved in the transmission of that information, the clearing process that determines amounts owing among participants, and the settlement of those amounts owing.

Developing Criteria for Payments System Access

The above discussion of the public policy objectives suggests that criteria for access to various elements of the payments system should be consistent with the goal of promoting an appropriate balance among the key objectives of efficiency, safety and the consideration of consumer interests. In general, efficiency may be advanced by encouraging competition as a means of providing payments services at the lowest possible price, and by creating market-driven incentives for innovation. An enhanced competitive environment may also generate benefits for consumers, including expanded choice and additional convenience, as well as potentially lower prices in the markets for payments services.

At the same time, however, the potential risks that participants bring to payment networks mean that broadened participation in clearing and settlement can result in higher costs associated with the co-ordination of activities, the monitoring of counterparties, and the identification and control of risks for both payments system participants and users. Such costs need to be considered in assessing the overall efficiency gains that new entrants might generate.

Thus, while broader access may provide benefits associated with increased competition, consideration must be given to the risks and responsibilities associated with different forms of participation, and involvement in different payments activities, in order to establish appropriate access criteria.

Box 2: ***Access to the Payments System in Canada – The Current Structure***

An important dimension of access to the payments system in Canada is membership in the Canadian Payments Association (CPA). Created under federal statute in 1980, the CPA plays a central role co-ordinating payments system activity and operates the national clearing and settlement system. Membership in the CPA is presently limited to federally and provincially regulated deposit-taking institutions (DTIs).

There are two categories of CPA members: Direct and Indirect Clearers. Direct Clearers maintain settlement accounts at the Bank of Canada. They clear and settle their own payments directly through the Automated Clearing Settlement System (ACSS) and, in turn, provide clearing services and access to settlement facilities for Indirect Clearers. To be eligible to act as a Direct Clearer, an institution must account for a minimum of 0.5 per cent of the total national clearing volume. Of the approximately 140 members of the CPA, only 13 are Direct Clearers: the Bank of Canada, eight banks, one trust company, two group clearers (which clear on behalf of the credit unions and caisses populaires) and one provincial government savings institution.

Currently, all transactions – retail and wholesale, paper and electronic – are settled through the same settlement network. When the CPA's new Large Value Transfer System (LVTS) begins operation later this year, the Bank of Canada will also provide settlement services to those CPA members that participate directly in the LVTS. The implementation of this system will result in the operation of two settlement structures: one primarily for small-value payments and another through which most large-value payment items will be handled.

While CPA membership is restricted to deposit-taking institutions, there are mechanisms through which non-DTIs may gain more limited forms of payments system access. For example, a non-DTI may allow its customers to make third-party payments by establishing a "sweep account" arrangement with a CPA member. To facilitate such an arrangement, a deposit account (on which the payment items will be drawn) must be established at the CPA member for each of the non-DTI's customers. Funds are then "swept" into the deposit account from the non-DTI as required to cover the customer's payments. Further, current rules allow the use of "payable-through" arrangements, in which a non-DTI would maintain a single account at a CPA member through which payments made by the non-DTI's customers would be processed. However, these arrangements have not traditionally been supported in the market, and the government has previously expressed reservations about their use, particularly by unregulated entities.

While the CPA plays a central role in the organization of payments activity in Canada, a number of other payment organizations operate outside its purview. For example, Interac operates Canada's only national ABM and EFT/POS networks; a number of credit card networks operate in Canada, the largest of which are the VISA and MasterCard systems; the Canadian Bankers Association is primarily responsible for the operation of the Interbank International Payments System (IIPS), through which many large-value payments are currently cleared; and the Canadian Depository for Securities Ltd. operates the principal clearing house for trades in securities. While these systems may provide initial clearing services to their members for payments originated within these networks, transactions generated through these systems eventually enter the CPA's clearing and settlement facilities for final settlement on the books of the Bank of Canada.

Access to these outside networks, and their rules of participation, are governed by the organizations themselves. While government exercises little direct control over these rules, all of these organizations are subject to Canadian competition law, which helps to ensure that the terms of access are reasonable and do not unduly constrain competition in the markets for these and related services. For example, under the terms of a Consent Order reached with the Competition Bureau in 1995, Interac agreed to loosen its membership restrictions, including allowing non-financial institutions to participate in the provision of certain network services. The agreement also required Interac to modify the structure of its board of directors and to change its pricing practices and the procedure for approving new network services.

Maintaining Confidence in the Payments Process

The process involved in the creation, clearing and settlement of payment items forms a chain of obligations linking the various participants in that process. For example, when a cheque is written by a customer and presented to a merchant as payment, the clearing and settlement process may involve the merchant's financial institution receiving the cheque and providing funds to the merchant, that institution entering the cheque into the clearings in order to obtain funds from the settlement agent acting on behalf of the customer's institution, the settlement agent obtaining funds from the customer's institution, and the customer's institution obtaining the funds from its customer.

Where there is a high probability that each party will meet its obligations, the process can be reasonably efficient and safe. However, the failure of any single participant in the chain has the potential to disrupt the process and impose losses on others. In order to maintain the level of safety and reliability needed to support public confidence in the payment system, restrictions on participation, as well as other risk controls, must operate to minimize the probability of failure and to mitigate its potential adverse effects.

For the payments process to be reliable, there must be reasonable confidence in the availability of funds in a payor's account, the integrity of technology and communications services linking the principal participants, and the ability of all institutions involved to settle any financial obligations arising from the clearing and settlement process.

Acquisition, Messaging, Clearing and Settlement Services

Payment services can be categorized according to the various stages at which they are provided in the payments process – acquisition, messaging, clearing and settlement. Acquisition and messaging services include the means by which the information needed to generate a payment is collected and transmitted within the payments system. Examples include the provision of ABM or point-of-sale (POS) terminals, supporting software and communications links, and the preliminary processing and transmission of payment records for entry into the clearings. Other essential elements of acquisition services are the provision of payment instruments to clients and the processes supporting the acceptance of those items as payments for goods and services. Clearing services relate to the process of verifying and sorting physical and electronic payments in order to calculate amounts owing among the various parties. Finally, settlement refers to the transfer of value between institutions to settle the obligations arising from payments processed in the clearings.

For the purpose of establishing appropriate access criteria for various elements of the payments system, a further distinction is also relevant, between participation in the provision of payment-related services that are simply inputs into the processing of payments, and those that may result in a participant being required to settle financial obligations with other participants. For example, at the acquisition level, the supply of POS terminals to merchants to capture payment information serves as an input into the payment process but does not generate a financial obligation on the part of the supplier of the terminal. Similar roles for service providers exist at the level of messaging services and in certain technical aspects of clearing and settlement. Participation in the provision of these types of services requires a high level of integrity and technical competence to ensure that payment processes are robust and reliable, but may not

require adherence on the part of providers to any special financial or regulatory standards. The ability to supply these services should thus extend to all firms that are able to meet the appropriate technical and operating standards.

Where participation in the provision of payments services gives rise to a financial obligation to other participants, prudential access criteria can serve as a means of providing some level of confidence that those obligations will be met. Within this broad category of participation, a range of different payment activities is possible, and it may be appropriate to set access criteria individually according to the activity. At least conceptually, the activities that belong in this category of participation can be separated into the following basic functions: the issuance of payments eligible for the clearings; direct participation in the settlement of one's own payments; and participation in the settlement of payments issued by other participants (i.e., the provision of settlement services to others).

In general, as one moves through these forms of participation, the consequences of a participant's failure to carry out its responsibilities become more widespread in terms of its potential effects on other participants. For example, if a direct participant in the settlement process also settles payments issued by other participants, not only will it have settlement obligations to other direct settling participants arising on its own behalf, but it could also have some responsibility for payment items drawn on those participants on whose behalf it acts.

The failure of any institution that issues payments, or is responsible for payment settlement, will also expose payees to potential losses. Further, the failure of an institution that settles other institutions' payments would be expected to have an impact on more payment recipients because of the volume of items funnelled through that participant.

The particular consequences of the failure of a participant to carry out its responsibilities will depend upon the nature of the activities in which it participates and the procedures governing any such failure. These procedures, as well as the arrangements that can be made between parties for controlling risk, may limit the adverse effects of some types of failures. They may also influence the nature of access criteria for different forms of participation.

General Criteria for Payments System Access

Regulation and Supervisory Oversight

The negotiation of a payment instrument in a deferred net settlement system – such as the CPA's Automated Clearing Settlement System – typically involves an implicit extension of credit from the institution receiving the payment to the issuing institution. In order for the receiving institution to willingly extend such credit in the absence of specific risk controls (e.g., collateralization or a third-party guarantee), it must be able to maintain confidence in the creditworthiness of its potential counterparties. Formal regulation and supervisory oversight represent an important signal in this regard, indicating that a participant is following reasonable guidelines for prudent behaviour – relating to both financial and other matters – and that some reputable body is formally charged with overseeing compliance with those rules.

The nature of payments system activity requires network participants to actively manage their net settlement obligations, arising from the flow of payments generated by their customers and the receipt of payment items drawn on other institutions. Adherence to appropriate solvency standards will generally help to guard against the risk that a participant will ultimately fail to meet its settlement obligations. Confidence in the solvency of participants, however, is not sufficient to ensure the smooth functioning of the clearing and settlement system, as the timing of payments is also of crucial importance. A requirement that payments system participants adhere to prudent and appropriate liquidity standards and practices helps to minimize the likelihood of payment failures. This, in turn, may promote reliability and public confidence in the system by helping to minimize the frequency of payment disruptions. The discretionary powers of the regulator to obtain relevant financial information from the entities it regulates, and its ability to monitor the solvency of institutions and take enforcement actions if necessary, further contribute to member confidence in the system's integrity.

The knowledge that payments system participants are governed by a rigorous regulatory regime is also important for maintaining user confidence in the soundness of the payments system. Such confidence will lead to broad acceptance of payment instruments by payees on relatively non-discriminatory terms, regardless of issuer. This, in turn, will allow consumers to maintain confidence that a payment item drawn on any particular payments system participant can be used as a convenient and reliable method of payment.

For these reasons, a formal regime of regulation and supervisory oversight should be considered an important prerequisite for access to the payments system. While all payments system participants should not be expected to adhere to identical regulatory standards, the regulatory framework applicable to each type of participant should be consistent with the nature of its business activities, assets and liabilities.

Access to a Reliable Source of Liquidity Support

During the normal course of business, financially solvent participants may, from time to time, find themselves with insufficient settlement balances to fully honour their outstanding payment obligations. In such instances, if a payment disruption is to be avoided, these institutions must have access to a reliable source of liquidity support. Further, since security is sometimes required in order to obtain liquidity (e.g., the *Bank of Canada Act* empowers the Bank to lend subject to certain conditions including the pledge of sufficient collateral), payments system participants should have the ability to create security interests in their property for the purpose of obtaining such loans.

Appropriate Legal Framework

The laws governing potential participants in the payments system would need to be compatible with the nature of payments system activities. Other payments system participants require legal assurances that the rights and obligations of a network member to clear and settle payments according to the by-laws and rules of the network can be satisfied, both in the normal course of business and in the event of a member's failure.

The legal framework governing the operation and activities of potential new participants would need to support any netting or loss-sharing agreements among payments system participants, and

to allow the pledging of collateral to clearing and settlement systems or providers of lender of last resort facilities, if necessary.

Further, in those instances in which a member becomes insolvent, the clearing and settlement network often imposes loss allocation rules. In order for participants to adequately assess their potential financial exposures, they must be confident that such loss allocation rules will be supported by the laws and regulations governing new participants.

Operational/Technical Capacity to Participate

Potential payments system participants would need to demonstrate the technical and operational capacity to undertake payment functions and to participate in clearing and settlement systems. More specifically, to minimize the risk of operational failure, protect the security of payments information, and maximize the efficiency with which payments can be cleared and settled, new participants would need to meet any reasonable operating standards – including technical standards on hardware, software, procedures and communications formats – imposed by payment networks on their members.

Further, standard time frames are often established within the clearing cycle for the verification and authorization of payment instructions. Time frames and procedures have also been established for the return of payment items that cannot be honoured, and for completing the settlement of payment for those items which cannot be returned (such as authorized debit card payments), to reduce uncertainty surrounding the finality of payment. Potential new participants would be expected to have the capacity to comply with any such time frames and procedures.

Broadening Payments System Access

Consistent with the goal of promoting broad competition in the provision of payment and related services, access to the payments system should be extended to all service providers that meet minimum objective criteria, as outlined in the previous section. As discussed earlier, these criteria are aimed primarily at achieving payments system efficiency, maintaining safety and soundness, and protecting the interests of consumers. While the application and relative importance of these general criteria may differ across payments system activities, they provide some relevant benchmarks against which potential new participants may be assessed.

To date, three classes of financial services providers have indicated to the Department of Finance a desire for more direct participation in the payments system: life and health insurance companies, investment dealers and mutual funds. The Appendix provides a brief overview of each of these types of institutions in the context of the general access criteria set out in the previous section, and outlines a number of outstanding issues with respect to each. A preliminary review of these institutions suggests that, while certain of the criteria may be satisfactorily met, a number of potentially significant issues remain to be resolved. Thus, the government should proceed with a detailed assessment of each of these potential participants with the goal of determining what forms of participation, including membership in the CPA, should be open to them.

Further, while the government does not exercise direct control over the terms of access set by payments systems and networks that operate independently from the CPA, it would be expected that these organizations would want to undertake a similar exercise to ensure that the broad framework governing access to the full range of payment and related services is as competitive as possible.

Finally, in its June 1996 White Paper, *1997 Review of Financial Sector Legislation: Proposals for Changes*, the Department of Finance indicated that, as part of its work on payments system issues, the Department would be exploring further its concerns over unregulated entities issuing payment items through payable-through arrangements. A conceptual overview of these arrangements suggests that both the processes and types of risks involved in clearing and settling the associated payment items are similar in many respects to those involved in clearing and settling payment items drawn on CPA members. This suggests that participation in payable-through arrangements should be subject to similar objective criteria as those established for more direct forms of payments system access. In addition, the current legal uncertainty regarding the rights and responsibilities of parties involved in transactions using payable-through drafts (e.g., with respect to the incidence of loss in the event of a failure) introduces certain risks that do not arise with cheques drawn on CPA members. Thus, if the use of payable-through drafts is to provide a viable form of payments system participation for regulated institutions, an effort should be made to address the existing legal uncertainties associated with their use.

4. Governance of the Payments System

Governance may be described very broadly as the means of achieving the public policy objectives identified for the payments system. More specifically, it involves the establishment of a legislative and decision-making structure that promotes the achievement of an appropriate balance among those objectives, not just in the current environment, but on an ongoing basis as the payments system evolves and as new technologies and new players emerge.

This section begins by describing briefly the range of alternative approaches to the decision-making structure for the payments system in terms of their mix of private and public sector involvement. It then considers areas in which the current structure could be enhanced and explores a number of specific approaches for bringing about these enhancements.

Approaches to Achieving the Public Policy Objectives

In examining alternative approaches to achieving the public policy objectives for the payments system, a fundamental consideration is the degree to which the provision of payments services and the formulation of rules governing the system are left to private participants or are undertaken by the public sector. In Canada, the overall approach to the organization of payments activities is to rely primarily on market forces but to provide a role for government where it can contribute to the achievement of a preferred outcome.

Consistent with this overall approach is the use of government intervention to address specific sources of tension between private incentives and the broader public interest. A number of such tensions may be identified for the payments system.

First, because the efficient provision and processing of payment services requires a high degree of co-operation among participants, there is a potential for the resulting co-operative arrangements to restrict competition unduly, either among participants or from outside. A related concern may arise from the fact that larger networks are often able to provide more highly valued services to users, and at a lower cost than smaller networks. Under such conditions, payment networks may gain significant market power or even monopoly status.

Second, government involvement may be used to address possible spillover effects resulting from the actions of individual payments system participants or co-operative groups. For example, individual participants might not always adopt clearing and settlement procedures that adequately control the spillover of risk to other participants in the payments system or to the rest of the economy. Accordingly, the public sector may choose to set certain standards aimed at limiting systemic risk and protecting payments system users from risk.

Finally, the public sector may provide services directly if it is particularly well qualified to do so, or if private sector provision of the service would raise concerns that could not easily be addressed by regulation. For example, given that efficiency considerations tend to support the provision of settlement services by a single provider, and given the desire to provide a risk-free asset for final settlement, central banks typically provide settlement services and determine the rules governing the provision of settlement accounts.

Models for Decision Making in the Payments System

The Payments System Advisory Committee considered four general models for decision making in the payments system, each representing a different mix of private and public sector involvement:

1) market participants make and implement decisions without public sector involvement;
2) market participants have primary responsibility for decision making, with broader input either from the public sector or through a process established by government;
3) a public sector body sets the rules governing market participants, possibly with input from the private sector; and
4) the public sector both sets the rules and provides services directly.

The extent and form of government intervention may vary for different parts of the payments system, reflecting the fact that the outcome of private actions will more closely parallel the desired balance among the public policy objectives in some parts of the payments system than in others. This will depend, for example, on the degree to which spillover effects, such as systemic risk, may be present and on the extent to which various activities are shaped by competitive and co-operative forces.

Governance of the Canadian Payments Association

The clearing and settlement services organized under the authority of the CPA are currently governed according to the second model described above. This model has the advantage of bringing to the decision-making process the experience of direct market participants, and their technical knowledge and understanding of the markets for payments services. At the same time, however, decisions made by direct participants may at times favour their interests and priorities over those of others affected by those decisions, including individual and corporate users of the payments system and providers of similar or related services. To deal with this potential shortcoming, the second model of governance provides the flexibility to incorporate broader input as well as public sector review and control.

The Payments System Advisory Committee generally felt that the current model, with some possible modifications, provides an appropriate balance between private sector activity and government involvement. Two key enhancements to this structure, however, were suggested: (1) strengthening the input of outside stakeholders into CPA decision making with the aim of aligning decisions more closely with the public interest; and (2) expanding the powers of the public sector to review, approve or veto decisions made by the CPA to help ensure those decisions are consistent with the public interest.

Aligning CPA Decisions More Closely with the Public Interest

The CPA's Mandate

The CPA's mandate should set out not only the scope of the CPA's activities, but also a set of objects or principles to help guide it in carrying out those activities. The CPA's mandate should thus include a responsibility to advance the public policy objectives identified for the payments system, namely, safety, efficiency and the consideration of the interests of consumers of payments services.

The core activities of the CPA are to establish, co-ordinate and/or operate national arrangements for the clearing and settlement of payments. To support these activities, the CPA must have the scope to set appropriate rules and procedures for the acceptance of items into the clearing and settlement process, and to stipulate the responsibilities of participants in those processes.

The CPA is also in a unique position to monitor emerging technologies in the payments system, including new payment methods, and to facilitate their development in a way that meets the public policy objectives. For example, the CPA could usefully set standards or guidelines that would encourage the interoperability of new payment methods, control risk, and provide appropriate levels of consumer protection. The CPA's mandate should thus include an explicit role in facilitating the development of new or emerging payment methods and activities. Such a role would tend to involve the CPA less actively in the forward-planning exercise, and more in integrating new developments, than is implied by the current mandate which calls on the CPA to "*plan* the evolution of the national payments system".

The Consultative Process

Consultations with non-CPA-member stakeholders and representatives of the public sector can help inform the CPA of interests outside their membership and thus contribute to the consideration of these interests in the decision-making process.

The CPA has established an extensive process of stakeholder consultation. Through a variety of forums, particularly the recently established Stakeholder Advisory Council, non-CPA-member stakeholders are kept informed of the CPA's corporate agenda including matters to be considered by the CPA Board. The functions of the Stakeholder Advisory Council include making recommendations to the CPA on the consultation process to be followed for individual projects of the CPA and, more generally, making submissions to the CPA Board as the Council sees fit.

While the consultative process has evolved and functions well on a voluntary basis, its effectiveness might be better assured if it were supported by a legislative requirement within the *Canadian Payments Association Act* (CPA Act). One approach might be to establish a legislative basis for the operation of the Stakeholder Advisory Council as a principal focus of the CPA's consultations with non-members. This would formalize the Council as the principal channel through which the concerns or views of any non-CPA member could be communicated to CPA management and the CPA Board.

Other elements of the current consultative process, including regular plenary meetings and the circulation of discussion drafts of rules prior to their approval by the CPA Board, help to ensure that information is available to interested parties beyond the Stakeholder Advisory Council and should be retained.

The current CPA Consultative Committee provides a formal vehicle for dialogue between the Department of Finance and the CPA Board. It is an essential element of public sector input under current arrangements, but may not be necessary if other forms of public sector input or oversight are provided.

CPA Board Structure

(i) Directors drawn from outside the CPA's membership

A strengthened consultative process can help ensure that stakeholders are aware of matters being considered by the CPA Board and that their views are known to Board members. However, without formal representation on the CPA Board, the influence of non-members over board decisions is likely to be limited.

This situation could be addressed by expanding the CPA Board to include directors drawn from outside the CPA's membership. A possible option would be to appoint independent directors drawn from the public at large. These directors would be "independent" in the sense of not being affiliated with any CPA member or particular group of non-member stakeholders. Their role would not be to represent a particular interest group, but rather to bring independent points of view to the consideration of issues before the Board and to the pursuit of the CPA's mandate.

An alternative approach would be to appoint representatives of key stakeholder groups to the CPA Board, such as consumers, corporate users, retailers, and providers of payment-related

services. If this approach were adopted, these directors could be expected to bring their particular perspective to the Board's discussions and decisions. However, like other directors, they would be expected to vote in accordance with the overall mandate established for the CPA. One possible means of organizing the appointment of such non-CPA-member directors would be to involve the Stakeholder Advisory Council in the selection process.

(ii) Public sector representation on the CPA Board

The CPA Act currently provides for public sector representation on the CPA Board by stipulating that an officer of the Bank of Canada serve as chairman. If the composition of the Board were changed to include directors drawn from outside the CPA, and if the public oversight of the CPA were strengthened along the lines discussed below, consideration would need to be given to the role played by a public sector representative on the CPA Board. Options to consider would include participation of a public sector representative as a regular director rather than as chairman, or perhaps as a member of the Board without voting rights.[1]

(iii) CPA member representation on the Board

Consideration should be given to moving away from the current approach of representation by institutional class (e.g., banks, trust and loan companies, centrals and other financial institutions). One option would be to structure the Board on the basis of members' form of participation in clearing and settlement processes. For example, under the current forms of participation, consideration may be given to representation from institutions that participate as Direct Clearers and Indirect Clearers (possibly with separate representation for those that participate in a group clearing arrangement). If other categories of participants were established as part of changes made in the area of access, separate representation on the Board would need to be considered for them.

Enhancing Public Sector Oversight

The kinds of changes contemplated above should help lead to decisions by the CPA that are generally consistent with the public policy objectives. However, these changes may not be sufficient on their own. Some form of strengthened government oversight may be needed, either in addition to the above changes or as an alternative to them, to ensure that an appropriate balance among the objectives is, in fact, reached. Effective oversight may also provide an added incentive for those involved in the decision-making process to consider the implications of their decisions on the public policy objectives.

Currently, the CPA Act requires that CPA by-laws be approved by the Governor in Council. This leaves open the potential for decisions with broad policy implications to be embodied in rules, over which the CPA Board has considerable discretion, provided they are consistent with the by-laws. While it is generally the case that CPA rules are technical in nature, consideration needs to be given to broadening the government oversight function in order to close this potential gap. One approach would be to simply extend the existing Governor-in-Council approval requirement to include CPA rules in addition to by-laws. A variant of this approach, which could lessen the burden on the approval process and minimize the potential for delays, might be

[1] Separate from the issue of public sector representation, it may be appropriate for the Bank of Canada to be represented on the CPA Board in light of the Bank's role as a participant in the payments system and as a provider of settlement services.

to exempt technical items if there was unanimous consent of the CPA Board, including independent and public sector directors.

Under either scenario, the increased volume of the CPA decisions that would be subject to review would require a commensurate increase in the resources devoted to the review and approval process. Otherwise, the process could both slow the CPA's ability to respond to changes in the payments system and fail to provide effective public sector oversight.

The level of resources and expertise required to support a review of CPA rules may suggest that the Governor in Council would no longer be best suited to undertake this role. An alternative may be to require that by-laws and rules be approved by the Minister of Finance. This new Ministerial function would need to be supported by staff within the Department. The choice of the Minister of Finance for this role would build on the Minister's current responsibility for the development of general policy for the payments system. A variant of this approach would be to provide the Minister of Finance with the power to issue a directive if, in the Minister's opinion, any course of action taken by the CPA was not in the public interest.

Alternatively, given the central position of the Bank of Canada in the payments system and the responsibilities of the Bank's Governor under the *Payment Clearing and Settlement Act* to control systemic risk, the Governor could be given the kinds of powers contemplated above for the Minister of Finance. This approach would have the benefit of bringing together the consideration of systemic risk issues and broader public interests so that a consistent policy approach to payments system issues could be developed.

It can also be argued that the range of policy concerns that arise in the operation of the payments system – including the level of competition, the spillover effects to the financial system and the rest of the economy, and the quality of services to users – suggests that the review function could benefit from expertise in all of these areas. There may also be advantages to involving those with knowledge of these issues in the decisions required of the review function. For these reasons, a small committee consisting of ex-officio members drawn from government agencies, such as the Department of Finance, the Bank of Canada and possibly others with relevant expertise, could be established to undertake the review process or to advise whoever has primary responsibility for carrying out the review.

Governance of Other Payments Systems and Networks

The discussion so far has focused on possible reforms to the CPA and to the process for reviewing the CPA's activities. This reflects the identification of the CPA as a central and essential facility in the payments system, as well as the only payments organization established pursuant to federal legislation. The settlement of ordinary payments on the books of the Bank of Canada is provided through CPA members exclusively, and CPA by-laws and rules determine eligibility of payment items for such clearing and settlement.

The assessment of other payments networks, including Interac for direct debit payments and shared cash dispensing, credit card networks, and emerging e-money networks, is more difficult. As noted above, there is a strong tendency for network externalities and scale economies to lead

to the emergence of dominant or single networks providing certain types of payment services. The scope of any oversight mechanism to cover payment networks outside of the CPA is an issue that requires further review. That being said, a potential advantage of establishing a public sector review body to oversee the activities of the CPA is that it would provide a vehicle for extending government oversight to other systems or networks if a decision were taken at a later date to so. A possible approach would be to set up a mechanism whereby the government could designate individual payments systems as being subject to a review process similar to that established for the CPA if it was considered to be in the public interest to do so.

Appendix: A Brief Overview of Potential New Participants

Life and Health Insurance Companies

Insurance companies are not permitted to accept deposits, though they do offer a number of products that may serve as close substitutes for deposits. Further, under the federal *Insurance Companies Act*, they are permitted to issue payment, credit or charge cards, and to participate in a payment, credit or charge card plan.

Many insurance companies offer a range of wealth management products, including annuities and segregated funds. Further, they may, in their normal course of business, generate significant volumes of payments to their customers (e.g., policy dividends and proceeds, annuity payments) and are permitted to retain certain of these funds on account. While further examination is needed into the nature of each of these types of accounts, these funds provide insurance company clients with balances that could potentially be accessible via the payments system.

Regulation and Supervisory Oversight:

Sources of Regulation:
Canadian life insurance companies may be incorporated at either the federal or provincial level. The Office of the Superintendent of Financial Institutions (OSFI) is the primary prudential regulator for federal institutions. The provinces in which these companies operate, however, are responsible for regulating certain aspects of their business and operations (e.g., sales practices, setting of rates and conduct of brokers).

Provincially incorporated life insurers are subject to regulation in the relevant provincial jurisdiction, though some provinces have contracted out their supervisory responsibilities to OSFI. While the regulatory frameworks are not identical from jurisdiction to jurisdiction, they are substantively similar in most areas. The remainder of the discussion in this section focuses on federally regulated insurers. Where differences exist between the federal and various provincial regulatory regimes, the impact of such discrepancies would need to be considered.

In addition to these domestically incorporated companies, a number of foreign insurance companies operate in Canada on a branch basis. These companies must be registered federally, and are subject to ongoing monitoring by OSFI. A more detailed examination of the regulatory and legal framework applicable to these companies is required to determine whether this framework would be suitable to allow branches of foreign companies to participate in the payments system on the same basis as is found appropriate for domestically incorporated companies.

Prudential Regulatory Standards:
Life insurance companies are generally well capitalised institutions, and are required to meet minimum regulatory capital standards. For federally regulated companies, these take the form of OSFI's Minimum Continuing Capital and Surplus Requirements (MCCSR). Under the MCCSR test, minimum capital is determined by applying risk factors to specific on- and off-balance sheet assets or liabilities and summing the results. Four categories of risk are considered: asset risk,

mortality/morbidity/lapse risks, interest margin pricing risk, and changes in interest rate environment risk.

Further, as a general principle, life insurance companies, like other federal financial institutions, are required by their governing statute to adhere to a "prudent person approach" to investment. In other words, they are required to adhere to investment and lending policies, standards and procedures that a reasonable and prudent person would apply under the same circumstances. Life insurance companies also face a number of specific investment and lending restrictions, as set out in the Insurance Companies Act, regulations and OSFI Guidelines.

In addition to these regulatory capital requirements, the life insurance industry, OSFI and Quebec's Inspecteur général des institutions financières (IGIF) have recently developed a set of Sound Business and Financial Practices, modelled after those promulgated by CDIC and applicable to its members. These standards deal with such areas as capital management, asset and liability quality, liquidity management, interest rate risk management and internal control. For federal insurance companies, OSFI has issued these standards as guidelines, and will be charged with monitoring and enforcing compliance.

Access to Liquidity Support:

A preliminary overview of the legal and regulatory framework under which Canadian insurance companies operate has not identified any obvious impediments that might prevent an insurance company from being able to obtain the liquidity support necessary to participate in the payments system.

As indicated in the text, collateral must often be provided in order to obtain liquidity support. Federally regulated life insurance companies, like other federal financial institutions, face a general prohibition on the creation of security interests in their property.[2] However, the Superintendent of Financial Institutions may, by order, approve the creation of security interests in specific classes of property, or up to certain dollar limits.[3] OSFI has issued an Interim Pledging Policy Statement that sets out the criteria for approving applications to create security interests, and establishes reporting and disclosure requirements. The criteria to be used by the Superintendent include the business reasons for the pledging of assets, the amount of pledging in relation to liquid assets and capital, and OSFI's evaluation of the institution's financial health. This policy statement applies equally to insurance companies and federal deposit-taking institutions.

Legal Framework:

Generally, life insurance companies are governed by a sound and comprehensive legal framework, as are other regulated financial institutions in Canada. Certain questions remain, however, where aspects of the legal framework are different from those applicable to existing payments system participants. An analysis of these differences is important to ensure that the framework governing potential new participants is compatible with existing rules and procedures employed in the operation of various elements of the payments system.

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[2] Deposit-taking institutions are permitted an exception for pledging to the Bank of Canada or to the Canada Deposit Insurance Corporation.

[3] The Superintendent also has the authority to make approvals on a case by case basis.

For example, under the federal *Winding-up and Restructuring Act*, in the event of the insolvency of an insurance company, the claims of policyholders rank ahead of those of other unsecured creditors. As a result, payments system participants could face significant losses in the event that a participating insurance company failed. The potential impact of the subordination of their claims on the willingness of payments system participants to grant payees provisional credit for payment items drawn on insurers (and thus extend unsecured intra-day credit to insurance company participants) would need to be examined.

As indicated above, insurance companies are not permitted to accept deposits. Whether this restriction raises issues in the context of payments system participation will need to be examined (e.g., whether the restriction might lead to larger net settlement obligations for insurance companies for a given scale of payment activities).

Investment Dealers

Clients of investment dealers may often have on account at the dealer free credit balances – the funds in a client's account in excess of the amount required to support his or her market positions.[4] These free credit balances represent funds payable on demand by the investment dealer, and are subject to restrictions on their use in the conduct of the dealer's business. These balances provide clients with a source of funds potentially accessible via the payments system.

Regulation and Supervisory Oversight:

Sources of Regulation:

Each province has passed legislation dealing directly with securities regulation. These laws apply to every trade, and to every person who trades, in securities or exchange contracts in the respective province. The legislation and accompanying regulations are enforced by the various provincial securities commissions.

Investment dealers are also subject to an extensive regime of self-regulation. The primary self-regulatory organizations (SROs) are the Investment Dealers Association of Canada (IDA) and the major Canadian stock exchanges. These organisations have been formally recognised as SROs by many of the provincial securities commissions, and are responsible for regulating the business conduct and affairs of their members. For recognized SROs, the securities commissions generally maintain the authority to, in the public interest, issue directives, orders, rulings and the like with respect to the by-laws, rules, regulations, policies and procedures of the SRO. The various SROs maintain largely uniform by-laws and rules and co-operate in regulating dealers that are members of more than one organization, contributing to a fairly uniform regulatory regime for investment dealers across Canada.

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[4] Under IDA regulations, the term "free credit balances" is defined to mean:

(a) for cash and margin accounts, the credit balance less an amount equal to the aggregate of (i) the market value of short positions and (ii) margin required pursuant to the regulations on those short positions; and

(b) for commodity accounts, the credit balance less an amount equal to the aggregate of (i) margin required to carry open futures contracts and/or futures contract option positions, (ii) less any equity in such contracts, (iii) plus any deficits in such contracts, provided that such aggregate amount may not exceed the dollar amount of the credit balance.

Prudential Regulatory Standards:
Investment dealers must comply with minimum capital requirements administered by both the provincial securities commissions and the various SROs. For example, under Ontario securities regulations, capital requirements are included as part of the conditions of registration. Under these rules, investment dealers must maintain minimum net free capital equal to $25,000 plus an amount proportional to their liabilities.[5] The IDA and the individual stock exchanges also impose varying minimum capital requirements on their members. In addition, the securities acts mandate the continuous and timely disclosure of financial and business information.

The IDA by-laws contain an Early Warning System designed to identify members in financial difficulty, based on their capital, profitability and liquidity positions. This system classifies troubled members into two categories, and imposes enhanced reporting and other requirements on such companies.

Finally, the IDA imposes minimum insurance requirements on its members to cover the theft, forgery or disappearance of securities.

Access to Liquidity Support:
A preliminary review of the laws and regulations applicable to investment dealers has not identified any legal impediments that might prevent an investment dealer from obtaining the liquidity support needed to support direct participation in the payments system. The ability of investment dealers to borrow sufficiently, and to pledge security in order to obtain such funds, however, will need to be ensured.

Legal Framework:
As indicated above, investment dealers are governed by provincial securities legislation, and by the rules of the various SROs. An examination of these rules is required to ensure that there are no legal impediments that might preclude investment dealers from participating directly in the payments system. For example, investment dealers are required at all times to adhere to the "know your client" aspects of securities rules. Such rules require the dealer to learn the essential facts relative to every customer and to every order or account accepted, and to ensure that the acceptance of any order is within the bounds of good business practice. Further consideration will need to be given to whether transactions initiated by clients through the use of various payment instruments would comply with the principles of the "know your client" rule.

Mutual Funds

A "mutual fund" is defined in provincial securities law as an issuer of securities that entitle the holder to receive on demand, or within a specified period after demand, an amount computed by reference to the value of a proportionate interest in the net assets of the issuer.[6] Unit holders of

[5] This variable amount is calculated as the sum of 10 per cent of the first $2.5 million of adjusted liabilities (liabilities less cash and near cash equivalents), 8 per cent of the next $2.5 million, 7 per cent of the next $2.5 million, 6 per cent of the next $2.5 million, and 5 per cent of adjusted liabilities in excess of $10 million.
[6] See, for example, *Ontario Securities Act*, Section 1.

mutual funds thus have access to assets that could potentially be used to back a range of payment instruments.

The Department of Finance has received separate submissions contemplating payments system access for mutual funds directly, and for mutual fund managers. The most recent material received from the mutual fund industry indicates that they believe the mutual fund itself is the entity most appropriate for participation. Thus, the following section assumes that the relevant question is whether mutual funds, as defined above, are suitable candidates for participation in the payments system. The appropriateness of this approach, however, should be considered open for discussion, and will need to be explored in greater detail.

It has further been suggested that payments system access be limited to money market mutual funds, on the grounds that other types of mutual funds are subject to significant levels of market risk, and that the ability to draw payments against such funds may be contrary to the long term nature of these investments. Further consideration of these views is necessary.

Regulation and Supervisory Oversight:

Sources of Regulation:

Mutual funds are subject to general trust and securities laws, enforced by the provincial securities commissions. Provincial securities acts and regulations contain provisions dealing with such areas as market integrity, business conduct and standard of care, disclosure, and contents of financial statements and prospectuses.

Mutual funds are also subject to regulation specific to the mutual fund industry. National Policy 39 (NP39) – soon to be replaced by National Instrument 81-102 and Companion Policy 81-102CP – adopted by the Canadian Securities Administrators, contains a comprehensive set of regulations governing the operation and activities of mutual funds. The provisions of NP39 cover such areas as investment practices and restrictions (including rules governing the use of derivatives), sales and redemptions, and new mutual funds and approvals for changes.

Other parties involved in the day-to-day operation of a mutual fund (e.g., dealer, advisor and custodian) are subject to various forms of regulation and registration requirements.

Prudential Regulatory Standards:

The primary focus of mutual fund regulation is to ensure that the key feature of a mutual fund is maintained – that is, that investors may redeem securities on demand.[7] While mutual funds are not subject to capital and liquidity requirements in the usual sense, the application of such requirements may not be appropriate given the nature of a mutual fund's business activities. More specifically, investment risk is borne by mutual fund unit holders, meaning that the value of a fund's liabilities, rather than being fixed, is closely tied to the value of its assets.

While they do not face formal capital or liquidity requirements, mutual funds are subject to minimum funding requirements at start-up, and to ongoing investment restrictions. Under NP39, the initial investment in a mutual fund must be at least $150,000, to be provided by the fund's

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[7] See Canadian Securities Administrators, "Notice of Proposed National Instrument 81-102 and Companion Policy 81-102CP".

manager, promoter, or other specified party. This initial investment may not be redeemed until an additional $500,000 has been received from other investors.

On an ongoing basis, a mutual fund must adhere to investment restrictions designed to promote portfolio diversification and liquidity, to help ensure that on-demand redemption requests can be satisfied. For example, under NP39, a mutual fund may not, without the approval of securities authorities:

- hold more than 10 per cent of its net assets in illiquid investments;
- hold more than 10 per cent of its net assets in the securities of any one issuer;
- hold more than 10 per cent of any class of securities of any one issuer;
- purchase real estate;
- purchase mortgages unless they are guaranteed or insured by the Government of Canada or a provincial government; or
- hold more than 10 per cent of its total assets in restricted securities.

Mutual funds also face tight restrictions on the use of derivatives.

Access to Liquidity Support:

Upon a cursory examination of the legal framework applicable to mutual funds, there do not appear to be any legal impediments to a mutual fund establishing a line of credit with a potential lender to provide emergency liquidity support to settle payment obligations. Although mutual funds are generally prohibited from borrowing, they are permitted to borrow on a short-term basis up to 5 per cent of their net assets (or such greater amount as may be authorized by regulatory authorities) to fund redemption requests, and are permitted to grant security on their assets.

Legal Framework:

Like investment dealers, mutual funds are regulated at the provincial level. An examination of the relevant provincial statutes and policies is necessary to ensure that mutual funds are not precluded from participating in any aspects of payments system activities. For example, like dealer transactions discussed above, purchases and redemptions of mutual fund units generated via the payments system may need to conform with the “know your client” aspects of securities laws.

While NP39 establishes procedures and timeframes for the execution of transactions involving the purchase or redemption of mutual fund units, such transactions could take up to five business days to settle.8 Further, NP39 requires only that the net asset value of a mutual fund for the purpose of the issue or redemption of securities of the fund be calculated at least once each week, with transactions implemented at a price equal to the net asset value next determined after the order is received. The possible implications of these settlement rules and procedures for the operation of the payments system will need to be considered to ensure that established clearing and settlement processes may be maintained.

Most mutual funds in Canada are organised as trusts, though some are established as mutual fund corporations. Further examination is needed to determine whether the legal framework applicable to mutual funds as trusts raises any concerns in the context of payments system

[8] Most money market fund transactions, however, settle on the date of the trade.

participation. Any issues arising from the differences in structure of mutual fund trusts and corporations will also need to be considered.