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Amendments to Pre-Authorized Debit (PAD) Agreement Requirements in Canada

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After a public consultation earlier this year, the anticipated amendments to the Canadian Payments Association's (operating as Payments Canada) Rule H1 – Pre-Authorized Debits (PADs) (Rule H1) came into effect on October 3, 2022.

Rule H1 requires a signed, written authorization from the payor of an obligation before issuing a pre-authorized debit against the payor's deposit account at another financial institution. Businesses debiting a customer's Canadian bank account (for personal or a business purpose) must have compliant PAD authorization agreements. The authorization agreement (i.e., the PAD agreement) must satisfy content requirements stated in Rule H1.

Transition Period

While the revised Rule H1 came into effect on October 3, 2022, a transition period (until December 31, 2023) has been provided to allow payees to implement necessary changes for compliance. During the transition period, both versions of Rule H1 will be in effect (i.e., the version preceding October 3, 2022, and the version in effect as of October 3, 2022) and available for reference on the Payments Canada website. On and after December 21, 2023, the revised Rule H1 requirements will apply.

The following summarizes certain key amendments in the revised Rule H1.

Electronic vs Paper Agreements

A welcome amendment to Rule H1 is the removal of the distinction between electronic and paper PAD agreements. Previously, Rule H1 required PAD agreements entered into electronically to additional verification requirements, including a minimum three-day lag before the first PAD.

The amendments to Rule H1 have removed the distinction between electronic and PAD agreements, such that agreements entered into in person and electronically are subject to the same requirements (i.e., there is no added procedure and onboarding time for electronic PAD agreements). The requirement to send a confirmation to the payor before the first debit has been removed, as well as the additional verification

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requirement to verify personal and/or banking information of the payor. As aptly stated by Payments Canada, this change will reduce onboarding time and facilitate the PAD process for businesses.

Commercially Reasonable

The definition of “commercially reasonable” has been revised to allow payees to use forms of verification tailored to the particular circumstances of their business and PAD arrangement - e.g., the circumstances of the PAD, their relationship of the payee with the payor, and the payee’s operational capabilities. Specifically, a payee must have procedures in place to verify the payor is who they purport to be, and these procedures must be reasonable and appropriate, having regard to the methods for verifying identity in general use for similar types of business and payment applications, and other commercial circumstances of the payor and the payee at the time the method is used. The revised Rule H1 includes the prior version’s examples of commercially reasonable methods.

Confirmation

A written confirmation of the PAD details is required to be provided to the payor at least 10 days *before* the first debit, though, if requisite waiver language is included in the PAD agreement, the confirmation can be provided within five days *following* the first debit. The confirmation can be in the form of the PAD agreement itself or a separate summary of key terms of the PAD agreement. Effectively, providing the payor with a copy of the PAD agreement would satisfy the confirmation requirement - i.e., a separate confirmation would not be required. A separate confirmation would be required in a scenario where a PAD agreement is entered into by telephone, for example, where all the required PAD disclosure may not be presented to the payor.

Use of a Payment Services Provider

If a payee is collecting payments on behalf of another entity that is providing the payor with goods or services, then the PAD agreement has to include a statement describing the arrangement between the payee and the entity providing the payor with the goods or services.

One-time PAD Agreement

One-time PAD agreements now automatically terminate once payment has been completed, and any subsequent PAD transaction will require a new PAD agreement.

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Optional Disclosure

Though not a prescribed requirement, PAD agreements may include a governing law and choice of forum clause, which is favorable for businesses operating outside of Canada and debiting Canadian bank accounts (subject to customary enforceability and other applicable legal requirements outside of Rule H1).

Additionally, a PAD agreement may outline the impact of terminating the underlying goods or services agreement related to the PAD agreement.

This publication is a general summary of the law. It does not replace legal advice tailored to your specific circumstances.