

Digital Policy Hub – Working Paper

Banking Without Banks: Policy Implications of Banking as a Service in Canada

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Key Points

- The emergence of banking as a service (BaaS) models is significantly transforming Canada's financial ecosystem by unbundling traditional banking, enabling technology companies to deliver financial products while regulated institutions maintain balance sheets and licences. This separation creates regulatory blind spots as customer relationships become disconnected from underlying banking operations.
- Consumers face significant protection gaps in BaaS arrangements, with the Canada Deposit Insurance Corporation (CDIC) deposit insurance coverage varying widely based on account structure. Most Canadians mistakenly believe financial technology (fintech) services offer identical protections to traditional banks, highlighting an urgent need for transparency reforms.
- Transparency in BaaS relationships is fundamental to market integrity and consumer protection. It empowers consumers to make informed decisions, promotes market discipline and ensures institutional accountability in line with democratic values. Without robust transparency standards, trust erodes, misconduct proliferates and the financial system faces heightened vulnerability to instability.
- Current regulatory oversight fails to address the distribution of banking functions across multiple entities, particularly when fintech companies influence lending decisions and money creation while operating outside traditional regulatory frameworks designed for unified banking institutions.
- Policy solutions must balance innovation with stability through standardized disclosures, joint liability mechanisms, and a shift to functional regulation that focuses on activities rather than entities. This adaptability is crucial for maintaining long-term financial stability and public confidence while enabling responsible evolution of Canada's financial services landscape.

Introduction

The financial services sector has experienced unprecedented technological disruption, with fintechs challenging traditional banking models through innovation in payments, lending and wealth management. Within this context, BaaS has emerged as a particularly significant development, representing a fundamental reconfiguration of the banking value chain that enables non-banking entities to offer banking services without holding banking licences. While these innovations create efficiency gains and expanded consumer choice, they simultaneously introduce novel regulatory challenges that existing frameworks may be ill-equipped to address. From a policy perspective, this evolution demands proactive, not reactive, regulatory engagement.

Canada's banking sector, renowned for its stability, operates under a robust federal framework governed by the Bank Act,¹ with prudential oversight from the Office of the Superintendent of Financial Institutions (OSFI)² and market conduct oversight from the

¹ *Bank Act*, SC 1991, c 46, online: <<https://laws-lois.justice.gc.ca/eng/acts/B-2/>>.

² *Office of the Superintendent of Financial Institutions Act*, SC 1987, c 11, online: <<https://laws-lois.justice.gc.ca/eng/acts/O-2.7/index.html>>.

Financial Consumer Agency of Canada (FCAC).³ This regulatory framework, historically designed around chartered banks, now confronts novel complexities as BaaS structures enabled by partnerships between fintechs and chartered banks allow non-bank entities to offer banking services without direct involvement in deposit taking or balance sheet management.

Additionally, in response to growing payment service providers (PSPs) operating outside traditional structures, Canada enacted the Retail Payment Activities Act (RPAA) in 2021,⁴ establishing regulations for payment service providers under Bank of Canada supervision.⁵ Similarly, the Consumer-Driven Banking Act (open banking framework)⁶ establishes rules for data sharing, with the FCAC overseeing consumer protections. Despite these efforts, gaps in consumer protection, liability clarity and systemic oversight persist, particularly for non-payment BaaS functions such as lending interfaces. Regulatory adaptation is critical to maintain the stability and trust that are cornerstones of Canada's financial system.

This paper explores: current structural and regulatory challenges in Canadian BaaS regarding consumer protection, liability and oversight; how comparable jurisdictions regulate BaaS; and actionable policy lessons for Canada to enhance consumer protection, clarify liability and ensure operational transparency in BaaS partnerships.

Conceptualization of BaaS

BaaS enables chartered banks to provide financial infrastructure and compliance services to non-banks, allowing them to offer banking products without a licence (Pineda 2025). It creates a layered ecosystem where banks offer infrastructure as a service, middleware forms the BaaS core and third parties integrate banking components (Skinner 2014). BaaS evolves from co-branded solutions to embedded finance, with fintechs such as neo-banks often becoming the primary customer interface (Deloitte 2021).

BaaS architecture reshapes risk profiles by separating customer relationships from balance sheet risks, enabling fintechs to offer services without equivalent regulatory oversight. Banks expose core functions, such as payments, lending and deposit taking through contractual agreements, integrating financial and non-financial entities (Bansal 2024; Stefanelli, Manta and Toma 2022). Fintechs influence credit decisions and embed services, indirectly affecting money creation while operating outside traditional regulation (Agarwal and Zhang 2020), raising concerns about risk allocation and regulatory gaps.

3 *Financial Consumer Agency of Canada Act*, SC 2001, c 9, online: <<https://laws-lois.justice.gc.ca/eng/acts/F-111/index.html>>.

4 *Retail Payment Activities Act*, SC 2021, c 23, online: <<https://laws.justice.gc.ca/eng/acts/r-7.36/page-1.html>>; the accompanying *Retail Payment Activities Regulations* were finalized in November 2023, detailing operational requirements for PSPs. Key provisions, including mandates for fund safeguarding, incident reporting and operational risk management, came into effect on September 8, 2025.

5 Supervised PSPs include entities involved in digital wallets, payment processing and other financial technologies.

6 *Consumer-Driven Banking Act*, SC 2024, c 16, s 1, online: <www.parl.ca/documentviewer/en/44-1/bill/C-69/royal-assent>.

Theoretical Foundations of Banking Functions

BaaS disrupts traditional banking by separating functions traditionally housed within a single entity. Patrick McDonald's (1971) insight⁷ that banking in Canada lacks a clear universal definition remains pertinent as fintechs perform bank-like roles without formal designation. Richard A. Werner's (2014, 2016) competing banking theories⁸ provide a framework for analysis, with the credit creation theory being particularly relevant for BaaS arrangements where the separation of customer relationships (managed by fintechs) from balance sheet activities (handled by banks) obscures the money creation process. This paper follows Werner's recognition of banks not as intermediaries, but rather as entities that create most of the money circulating in the economy when they issue new loans.⁹

Robert C. Hockett and Saule T. Omarova's (2017) "franchise view" sees finance as a public-private partnership, with banks as chartered utilities using public goods like deposit insurance. Fintechs in BaaS extend this franchise, relying on banks' licensed status while distributing services. This raises moral hazard and accountability issues, as fintechs benefit from trust in regulated banks but may evade full oversight (Hockett and Omarova 2017).

State of the BaaS Landscape in Canada

Canada's BaaS ecosystem continues to develop, with players adapting BaaS principles to Canada's unique financial market. Table 1 outlines major fintechs and their licensed partners. This symbiotic arrangement expands consumer and business financial product choices but raises regulatory and consumer risk questions.

7 McDonald (1971, 124) suggests that "banking can be either a broad term or a very narrow one; no single, universally accepted definition can be found in the literature of economics or the opinions of the courts."

8 Werner (2016) outlines three competing theories of banking. First, the financial intermediation theory views banks as passive channels that direct existing savings from depositors to borrowers. In this perspective, banks are not fundamentally different from other financial intermediaries such as mutual funds, as they simply facilitate the movement of existing capital. Second, the fractional reserve theory, while still viewing banks as intermediaries, recognizes their collective ability to expand the money supply through the multiplier effect under a reserve system. Although an individual bank cannot create money independently, the banking system as a whole can amplify credit and deposits by repeatedly lending deposited funds. Third, the credit creation theory presents a significant departure from the others by asserting that individual banks create money when they issue loans. They simultaneously generate matching deposits without relying on prior savings.

9 In modern economies, the bulk of money is created by commercial banks when they extend new loans. The amount of money created in the economy ultimately depends on the monetary policy of the central banks, through interest rates and sometimes through direct asset purchases (quantitative easing) (McLeay, Radia and Thomas 2014).

Table 1: Key Risks and Ethical Consideration Guidance Provided in Policies

Company	Description and Banking Offering	Licensed Partners
Neo Financial	High-interest savings, credit cards	ATB Financial, Peoples Bank of Canada, Concentra Bank (now part of Equitable Bank)
Wealthsimple	Spending account, prepaid Visa card	Funds in trust with multiple CDIC member institutions
Koho Financial	Prepaid Visa cards, savings account.	Peoples Trust
Synctera	BaaS platform for accounts and cards	Funds in trust with one or more CDIC member institutions
Float Financial	Corporate cards, spending management tools	Peoples Trust Company
Bloom Finance	Card for seniors, secured against home equity	Peoples Trust Company
Keep	Corporate credit cards, virtual cards, expense dashboard	Peoples Trust Company

Source: Author's elaboration, based on news, LinkedIn profiles, Pitchbook and Crunchbase.

Note: See Table 3 for examples of CDIC protection disclosures.

Regulatory Gaps and Policy Challenges

The BaaS structure creates complex relationships where compliance, risk management and consumer protection responsibilities can be fragmented or unclear (Mdluli, Jeník, and Zetterli 2022)). This partnership model reduces market entry costs for fintechs but introduces third-party dependencies and regulatory risks into the banking system (Lorentz, Smith and Rovira 2023). The existing framework wasn't designed for these hybrids, creating oversight gaps that could undermine confidence in the system and exacerbates the historical "inextricable confusion" in Canadian regulatory authority (McDonald 1971). As fintech-bank partnerships continue to outpace regulatory development in Canada, they could expose some of the following regulatory gaps.

Deposit insurance clarity: A significant gap exists in understanding CDIC coverage in BaaS arrangements, as fintechs are not CDIC members, and protection depends on the nature of their partnerships with member banks. A recent by-law¹⁰ aims to strengthen trust account oversight by requiring member institutions and trustees, including fintechs acting in a trustee capacity, to maintain detailed beneficiary records. However, end-users still cannot verify whether fintechs meet these requirements, creating a gap in public assurance. Customers often face significant risk confusion relating to deposit insurance status, falsely assuming protection against fintech failures, a misconception seen in the United States (Azarow and Toomey 2022).

10 Canada Deposit Insurance Corporation Co-Owned and Trust Deposit Disclosure By-law (SOR/2019-312), online: <<https://laws-lois.justice.gc.ca/eng/regulations/SOR-2019-312/index.html>>.

Three coverage scenarios exist: pooled account — only the fintech is covered as the depositor, leaving clients unprotected in fintech insolvency; trust account — CDIC protects up to CDN\$100,000 per beneficiary, contingent on proper documentation; and direct client account — standard CDIC coverage applies. Although the CDIC provides information guidelines under its Deposit Insurance Information By-law,¹¹ inconsistent disclosure practices across institutions continue to mislead consumers (Table 3).

Consumer protection: Fintechs offering bank-like services often operate outside established consumer protection frameworks (Dall 2025). An FCAC survey found most Canadians incorrectly believe they receive the same protections with fintechs as with traditional banks (FCAC 2023, 5). While consumers retain some protections through the underlying bank and provincial rules, the lack of direct oversight of the fintech interface creates significant regulatory gaps.

Liability ambiguity: Current regulations fail to clearly address liability issues. In the case of a fintech’s technical error that may cause losses or data breaches, responsibility between the fintech and the bank can be unclear, and customers may find themselves caught between parties deferring responsibility to each other. This accountability vacuum is exacerbated by complex partnership structures where fintechs handle user interfaces and customer onboarding. While OSFI’s (2023) “Third-Party Risk Management Guideline” states that federally regulated financial institutions bear ultimate responsibility for outsourced functions, the practical implementation of this principle remains opaque to consumers.

Indirect money creation: Some fintechs in BaaS arrangements contribute to indirect money creation. For example, some fintechs are extending margin lending¹² allowing clients to borrow against investments, providing additional liquidity and contributing to credit creation. Similarly, unsecured credit cards, indirectly affect money creation when partner banks issue loans or receivables.

RPAA consumer protection gaps: The RPAA improves payment services oversight but leaves some consumer protection gaps. While PSPs must safeguard user funds through private insurance or guarantees,¹³ this “equivalent insurance” mechanism creates weaker protection compared to traditional banking deposits. Private insurance arrangements may prove inadequate during crises or stress scenarios. Additional limitations include the absence of clear liability rules for unauthorized transactions, lack of standardized disclosure formats, and no specific consumer complaint procedures. While Bank of Canada risk management and funds safeguarding requirements are scheduled in the last quarter of 2025¹⁴ and implementation may address some issues, its current focus on operational resilience and fund safeguarding neglects comprehensive consumer protection standards.

11 Canada Deposit Insurance Corporation Deposit Insurance Information By-law, online: <<https://laws.justice.gc.ca/eng/regulations/SOR-96-542/index.html>>.

12 Margin lending involves direct balance-sheet lending by Wealthsimple Investments Inc., a regulated investment dealer overseen by the Canadian Investment Regulatory Organization and subject to Canada’s securities regulations, ensuring compliance with margin requirements and investor protections.

13 The RPAA mandates that PSPs protect these funds through private insurance or guarantees, which must cover an amount equal to or greater than the total end-user funds held by the PSP, and these funds must be kept in a separate account dedicated solely to this purpose. The insurance can be obtained from a recognized insurance provider, or a guarantee can be secured from a financial institution (Bank of Canada 2025).

14 Risk management and funds safeguarding requirements take effect September 8, 2025. See www.bankofcanada.ca/core-functions/retail-payments-supervision/retail-payments-supervision-key-milestones/.

Table 2: CDIC Deposit Protection Scenarios for Fintechs Managing Funds

Scenario	CDIC Coverage	Implications in Case of Failure	Scheme of CDIC Coverage
Fintech holds funds directly (pooled account)	No CDIC protection for clients' funds.	Fintech failure: client funds at risk in bankruptcy. Bank failure: CDIC covers only the fintech, not the clients.	The member institution has no information on the clients
Fintech account in a trust (client as beneficiary)	Up to CDN\$100,000 per beneficiary, contingent on documentation.	Fintech failure: funds in trust protected. Bank failure: CDIC reimburses each beneficiary up to CDN\$100,000.	CDIC coverage protection beneficiary of a trust
Account in client's name (CDIC member Institution)	Up to CDN\$100,000 per insurance category.	Fintech failure: funds are safe. Bank failure: CDIC reimburses up to CDN\$100,000 per category.	CDIC coverage within one coverage category

Source: Author, based on information from CDIC's website. See www.cdic.ca/depositors/whats-covered/fintechs.

Table 3: Snippets of Corporate Disclosures of CDIC Protection in Selected Fintechs

Financial Institution	Corporate Disclosures
Neo Financial www.neofinancial.com/legal/privacy-policy	The Neo Everyday and Neo High-Interest Savings accounts are provided by Peoples Bank of Canada , a CDIC member institution, and are eligible for CDIC deposit protection. Deposits held in Neo Everyday and Neo High-Interest Savings accounts are combined with eligible deposits held at Peoples Bank of Canada for up to \$100,000 of deposit protection per category, per depositor.
Wealthsimple https://help.wealthsimple.com/hc/en-ca/articles/14905388487579-Understand-how-CDIC-coverage-works-in-your-Cash-account	The funds in all of your individual and joint Cash accounts are placed in trust with multiple schedule 1, CDIC-member, regulated Canadian financial institutions . CDIC protection against the failure of these banks extends to Wealthsimple Cash account holders for up to \$1,000,000 CAD across all Cash accounts. We have partnered with a number of CDIC-member, Canadian Financial Institutions to take advantage of a combined CDIC-eligible coverage amount (up to \$1,000,000 CAD) for our clients across all of their Cash accounts.
Koho Financial www.koho.ca/	When you opt in to Earn Interest, your funds are placed in trust with one or more CDIC member institutions . Funds held in trust by CDIC member institutions are eligible for CDIC protection of up to \$100,000 per beneficiary, per member institution, if the member institution were to fail.

Source: Corporate websites. Disclosures text directly retrieved from the financial institutions' public websites.

International Regulatory Approaches to BaaS

Different jurisdictions offer instructive approaches to BaaS regulation. The European Union leads with a comprehensive framework including the second Payment Services Directive (PSD2), which lays down the foundation for open banking,¹⁵ and sets rules for third-party providers (European Central Bank 2018). The principle that licensed institutions cannot outsource compliance responsibilities remains central.¹⁶ The European Banking Authority's "same activity, same risk, same rules"¹⁷ approach ensures consistent oversight (European Banking Authority 2017), while the Digital Operational Resilience Act (DORA),¹⁸ strengthens third-party risk management.

In the United Kingdom, the Open Banking Implementation Entity oversees open banking standards implementation in compliance with the Competition and Markets Authority (CMA) Order¹⁹ and PSD2. The Financial Conduct Authority's (FCA's) Consumer Duty standards²⁰ strengthen protection across financial services by requiring firms to prioritize customer outcomes, even for services influenced by third-party providers (FCA 2022). The Critical Third Parties (CTPs) regime²¹ focuses on resilience of key service providers crucial to the financial system (Bank of England 2024).

The United States has developed joint guidance through federal agencies. The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation (FDIC) and the Office of the Comptroller of the Currency (OCC) issued joint third-party risk management guidance²² highlighting risks in bank arrangements for deposit products (Board of Governors of the Federal Reserve System, the FDIC and the OCC 2024). The agencies also published a request for information²³ seeking input on bank-fintech arrangements and their risk management practice. They warn consumers may not realize deposit insurance does not cover third-party failures, with the FDIC focusing increasingly on false advertising of deposit insurance with revisions to the False Advertising Rule (*ibid.*).²⁴

15 Open banking is a model that allows third-party providers to access customers' banking information, with their explicit consent, to develop personalized financial products and services even when those customers maintain their primary accounts with different banking institutions (Eccles, Grout and Siciliani 2019; Bank for International Settlements 2019).

16 EC, *Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market, amending Directive 2002/65/EC, 2009/110/EC and 2013/36/EU and Regulation (EU) No 1093/2010, and repealing Directive 2007/64/EC* [2015] OJ L 337, art 19.

17 The principle of "same activity, same risk, same regulation" advocates for the need to move from an entity- to an activity-based approach to financial regulation, which means that financial services carrying similar risks should face equivalent regulatory treatment regardless of provider type (Pacheco 2021).

18 Implemented on January 17, 2025, DORA strengthens digital resilience in the financial sector by enhancing institutions' ability to withstand, respond to and recover from information and communication technology (ICT) disruptions. It harmonizes operational resilience rules across 20 types of financial entities and their ICT third-party service providers.

19 In 2017, the CMA ordered the nine largest UK banks to implement open banking standards.

20 On July 27, 2022, the FCA published the Policy Statement 22/9 *A New Consumer Duty - Feedback to CP21/36 and final rules* (PS22/9) with accompanying guidance (FG22/5).

21 On November 12, 2024, UK regulators published statements on CTP identification, designation recommendations to HM Treasury, fundamental rules, operational requirements, incident reporting, oversight and enforcement.

22 On June 9, 2023, federal agencies issued guidance to help banks manage risks in third-party relationships, including fintechs, by aligning practices with the nature and risk profile of these partnerships.

23 *Request for Information on Bank-Fintech Arrangements Involving Banking Products and Services Distributed to Consumers and Businesses*, 89 Fed Reg 61577 (2024).

24 *Ibid.*

Conclusions

BaaS drives innovation and consumer choice but challenges Canada's regulatory framework by splitting banking functions across entities with varying levels of regulation. Gaps in consumer protection, deposit insurance clarity, liability and systemic oversight risk eroding trust and financial stability. Canadian policy makers must adapt regulations to balance fintech innovation with robust risk management.

Recommendations

Enhance Transparency and Consumer Protection Standards

The disaggregation of banking services must preserve consumer rights. Building trust requires robust, consistently applied standards, underpinned by transparency through the following measures:

- **Standardized disclosures:** The FCAC should mandate clear disclosures detailing the roles of fintechs and partner banks, clarifying CDIC eligibility for different account types and including mandatory public attestations or easily recognizable “CDIC compliant trustee” labels.
- **Market-conduct supervision:** Extend consumer protection provisions overseen by the FCAC, such as rules against deceptive practices,²⁵ to fintechs performing bank-like services. While consumer protection falls under provincial jurisdiction over property and civil rights,²⁶ FCAC's mandate could be clarified to cover federally regulated financial functions performed by fintechs in BaaS partnerships through a federal-provincial cooperative framework.
- **Extending conduct rules functionally:** The FCAC's oversight should extend to fintechs in partnership arrangements with federally regulated financial functions, including complaint handling and error resolution similar to the “Code of Conduct for the Credit and Debit Card Industry.”²⁷
- **Improving regulatory transparency:** Enhance supervisory reporting requirements for federally regulated institutions involved in BaaS. Banks should provide detailed reports outlining third-party partnerships, services offered, key metrics and risk indicators (for example, number of end-users, transaction volumes, deposit balances held via BaaS). The OSFI could update Guideline B-10 to specify these requirements.

25 The Unfair or Deceptive Acts or Practices Rule is regulated by the Financial Services Regulatory Authority of Ontario. It defines unfair practices in the insurance industry and aims to enhance consumer protection. See www.fsrao.ca/regulation/rules/unfair-or-deceptive-acts-or-practices-rule.

26 Provincial consumer protection legislation covers various aspects, such as credit reporting, debt collection practices, and the sale of financial products. See <https://ised-isde.canada.ca/site/office-consumer-affairs/en/complaint-roadmap/consumer-protection-legislation-canada>.

27 The Canadian Code of Practice for Consumer Debit Card Services outlines industry practices and consumer protections related to electronic funds transfers. See www.canada.ca/en/financial-consumer-agency/services/industry/laws-regulations/debit-card-code-conduct.html.

- **Exploring the role of standards bodies:** Develop collaboration with standards organizations such as the Canadian Standards Association to establish technical standards for application programming interface protocols and cybersecurity that align with regulatory frameworks.

Establish Joint Liability Mechanisms

Financial regulators should introduce a joint liability regime for fintech-bank partnerships, where both share legal accountability for the integrated service experienced by consumers. This mechanism, potentially overseen via the OSFI's third-party risk management guidelines (such as Guideline B-10), should require partnership agreements to include specific clauses defining shared accountability and responsibilities for handling specific failure scenarios. A formalized coordination mechanism should be established among federal and provincial regulators, including the OSFI, the FCAC and the Financial Transactions and Reports Analysis Centre (known as FINTRAC), provincial securities commissions and the CDIC to develop unified policy approaches and balance innovation with financial stability.

Adopt a Functional Regulatory Framework

Since BaaS models disaggregate activities traditionally performed by a single licensed institution, entity-based regulation alone is insufficient. Regulators should move toward a functional activity-based framework where entities engaging in bank-like activities are subject to appropriate regulation proportional to its risks, regardless of which entity performs it (Pacheco 2021). Following the principle of “same services, same risks, same rules,” authorities aim to ensure any firm offering a given financial service faces comparable requirements, reducing systemic and consumer protection risks (Borio, Claessens and Tarashev 2022).

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Acronyms and Abbreviations

BaaS	banking as a service
CDIC	Canada Deposit Insurance Corporation
CMA	Competition and Markets Authority
CTP	Critical Third Parties
DORA	Digital Operational Resilience Act
FCA	Financial Conduct Authority
FCAC	Financial Consumer Agency of Canada
FDIC	Federal Deposit Insurance Corporation
fintech	financial technology
ICT	information and communication technology
OCC	Office of the Comptroller of the Currency
OSFI	Office of the Superintendent of Financial Institutions
PSD2	second Payment Services Directive
PSPs	payment service providers
RPAA	Retail Payment Activities Act

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