

*Electronic Presentment of Cheques in Canada: Digital Official
Images of Eligible Bills*

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1. Introduction

Sometime before the end of 2008 all Canadians and their legal advisors are going to have to adapt themselves, and their record-keeping and related practices, to the fact that the originals of all cheques will no longer be made available by their banks after they have been presented for payment. Amendments to the *Bills of Exchange Act*¹ which came into force on April 20, 2007 will authorize banks and other financial institutions that provide chequing services to their customers through the facilities of the Canadian Payments Association (CPA),² to capture a digital official image of the front and back of each cheque deposited with them, and to destroy the original instruments within a short time thereafter. The official image will take the place of the original document for all purposes. The new sections of the Act, and complementary changes to the CPA's rules for the cheque-collection system, will make cheque "truncation"³ the norm, rather than a limited practice by a few credit unions and trust companies, as has been the case until now. It will accordingly require some changes in the laws of evidence and in administrative practices regarding proof of payment. This comment reviews the text of the new provisions of the Act with a view to explaining rather than critiquing the new regime. It is based in part on material that I provided as counsel to the federal government, and also in part on other material that is to appear in my forthcoming treatise, *The Law of Banking and Payment in Canada*.⁴

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¹ R.S.C. 1985, c. B-4 [the Act].

² I deal with "on-us items" *infra* note 35 and accompanying text.

³ This is an American term, defined as denoting any process of cheque collection that arrests or stops the movement of the physical cheque at some point in the chain of affected banks before it is returned to the drawer, and substitutes an electronic message or image of some sort. See Donald I. Baker and Roland E. Brandel, *The Law of Electronic Funds Transfer Systems*, 2d ed. (Boston: Warren, Gorham & Lamont, 1988) c. 2 at 2(1)ff; Henry J. Bailey and Richard B. Hagedorn, *Brady on Bank Checks*, 7th ed. (Boston: Warren, Gorham & Lamont, 1992) at para. 1.24.

⁴ To be published in looseleaf format by Canada Law Book in 2008.

2. *The Business Case for Digitizing Cheques for Electronic Presentment*

The Honourable Jim Flaherty, Minister of Finance in the current government, introduced the enabling amendments to the *Bills of Exchange Act* as part of an omnibus financial services bill⁵ on December 7, 2006 by telling Parliament:

One way that this bill will improve our financial system is by allowing for the implementation of electronic cheque imaging. Currently, banks process about one billion paper items, mostly cheques, annually, valued at over \$3 trillion. The process of clearing a cheque includes the physical delivery of the cheque to the paying or issuing financial institution in order for it to decide whether or not to make the payment. This process is more labour intensive, time consuming and costly than necessary, particularly given today's developments in technology. The proposal in this bill to allow for the implementation of electronic cheque imaging will result in significant efficiency gains, saving time and resources currently dedicated to the transport of cheques. This will allow banks to keep their costs down, a benefit that needs to be passed on to customers to ensure that the efficiencies derived from electronic cheque imaging will be shared by all users of the payment system.⁶

A fuller statement of the business case for ceasing to present each cheque physically to the branch of the depository financial institution that administers the account on which it is drawn is provided by the report of the Canadian Payments Association, *Cheque Imaging in Canada: A Change Whose Time Has Come*.⁷ The main arguments of the authors of the report were the greater speed and efficiency (including lower cost) of electronic collection, as well as the creation of a new platform on which banks might base new customer reporting and accounting services. While the depository financial institutions were the prime movers for change, their arguments evidently convinced an impressive number of organizations to support their initiative. Endorsing representations were made to Finance Canada not only by business organizations, such as the Canadian Chamber of Commerce, the Retail Council of Canada, the Treasury Management Association of Canada, and the Federation of Independent Business, but also professional organizations such as the three

⁵ Bill C-37 of the 1st session of the 39th Parliament.

⁶ *House of Commons Debates*, No. 093 (7 December 2006) at 1150 (Hon. Jim Flaherty).

⁷ Canadian Payments Association, *Cheque Imaging in Canada: A Change Whose Time Has Come*, (March 2007), online: <http://www.cdnpay.ca/publications/pdfs_publications/imaging.pdf>.

associations representing the Canadian accounting profession, and – perhaps more significantly – the Consumers’ Association of Canada.⁸

3. *The Need for Enabling Legislation*

Notwithstanding the strong business case, and the documented support of many influential associations of important classes of customers and other interested persons, the industry has felt unable to implement electronic collection procedures due to the lack of support from their legal advisors⁹ and the absence of enabling legislation, such as had been enacted in the United Kingdom, the United States and Australia, among others.¹⁰ I have discussed these issues at some length elsewhere,¹¹ grouping them for this purpose into four classes: (1) bills of exchange issues; (2) evidentiary issues; (3) professional accounting (“audit trail”) issues; and (4) bureaucratic (“administrative procedure”) issues.

The bills of exchange issues all proceeded from the significance that the law of bills of exchange historically placed on possession of the original instrument as a condition precedent to the enforcement of it by the holder.¹² Presentment of a cheque for payment by the transmission to the drawee of only an image of it seemed to flout the clear requirement of section 84(3) of the *Bills of Exchange Act* that the holder “exhibit the bill” to the person from whom payment is demanded. In addition, there was a concern that, if a cheque were to be destroyed following the capture of the image or data presented in it, a court might conclude that it had been “cancelled” within the meaning of section 142 of the Act, such that the drawer would be discharged; “materially altered within the meaning of sections 144 and 145, such that it would be voided; or “lost” within the meaning of section 156, and so require an indemnity to be provided by the ex-holder before action could be brought to enforce it. Enabling legislation

⁸ See Canadian Payments Association, *Cheque Imaging: Stakeholder Support*, (December 2006), online: <http://www.cdnpay.ca/news/pdfs_news/stakeholder_support_cheque_imaging.pdf> (setting out excerpts from letters and briefs from May and June 2005).

⁹ Benjamin Geva has reviewed the issues that arise in the absence of enabling legislation in “Off-Premises Presentment and Cheque Truncation under the *Bills of Exchange Act*” (1987) 1 B.F.L.R. 295.

¹⁰ See Benjamin Geva, “Recent International Developments in the Law of Negotiable Instruments and Payment and Settlement Systems” (2007) 42 Tex. Int. L. J. 685.

¹¹ Bradley Crawford, *Payment, Clearing and Settlement in Canada* (Aurora, Canada Law Book, 2002) c. 9 at 5ff [Crawford, *Payment, Clearing and Settlement*].

¹² See *Bills of Exchange Act*, *supra* note 1, s. 73 (“rights and powers of holder”) and s. 2 (“holder” means the payee or endorsee of a bill or note who is in possession of it, or the bearer thereof...”).

appeared to be required to prevent the accidental application of the old law to the prejudice of the public.

The evidentiary issues were largely procedural rather than substantive. The *Canada Evidence Act*¹³ establishes the admissibility of electronic documents, but places on the person tendering such a document “the burden of proving its authenticity by evidence capable of supporting a finding that the electronic document is that which it is purported to be.” In many provinces, the *Evidence Act* contains an identical provision, or one to the same effect.¹⁴ There was a risk that if the payment system participants routinely destroyed a million cheques each night, the pursuit of a significant number of civil actions could well be complicated and delayed by the need for courts to review foundation evidence as to the operation and reliability of the new systems to produce images of instruments offered in evidence. In addition, the possibility of other difficulties arising under provincial evidence legislation was confirmed by provisions such as section 34(3) of the Ontario *Evidence Act*¹⁵ which at one time gave the courts of that province a discretion to exclude a microfilmed image of a cheque that had been destroyed less than six years after the payment transaction had ceased to be regarded as current – an uncertain length of time. The new provincial *Electronic Commerce Acts*¹⁶ appeared not to offer any more reliable or convenient approaches to these issues, since they typically refer to documentary requirements that arise under provincial legislation or to documents subject to provincial jurisdiction which, of course, could have no application to cheques on grounds of constitutional law. The federal equivalent, the *Personal Information Protection and Electronic Documents Act*,¹⁷ offered no new approach either.

The “audit trail” and “administrative procedure” obstacles to the substitution of digital images for cheques are somewhat harder to document and, in any event, mostly irrelevant now, though a number of such restrictions on the use of copies of payment instruments are outlined in *Crawford and Falconbridge*.¹⁸ The change in the approach with respect

¹³ R.S.C. 1985, c. C-5, as amended by S.C. 2000, c. 5, s. 56.

¹⁴ See e.g. R.S.O. 1990, c. E.23, s. 34.1(4); R.S.A. 2000, c. A-18, s. 41.3; S.S. 2006, c. E-11.2, s. 55; R.S.Y. 2002, c. 67, s. 3.

¹⁵ R.S.O. 1990, c. E.23, as rep. by s. 34.1 by S.O. 1999, c. 12, Sched. B, s. 7.

¹⁶ See e.g. *Electronic Commerce Act, 2000*, S.O. 2000, c. 17; and the equivalent provisions in: S.N.S. 2000, c. 26, s. 3(4); S.N.L. 2001, c. E-5.2, s. 4(1)(e); S. Nu. 2004, c. 7, s. 3(3)(e).

¹⁷ S.C. 2000, c. 5, 1-2.

¹⁸ Bradley Crawford and J.D. Falconbridge, *Banking and Bills of Exchange*, 8th ed. (Aurora: Canada Law Book, 1986) c. 38 at 93ff.

to these issues is perhaps best evidenced by the fact that the Department of Finance sponsored Bill C-37 as a government bill, the Minister introduced it, and it received written support from the three national professional associations of accountants. Perhaps the fair conclusion would be that the previous opposition to the use of informal copies of payment instruments was based on the lack of any firm legal foundation for accepting anything other than the original as proof of payment. With the enactment of Bill C-37, that objection was removed, and should not remain problematic for anyone else, either.

4. Bill C-37

Bill C-37 was entitled “*An Act to amend the laws governing financial institutions and to provide for related and consequential matters.*” It was introduced on November 27, 2006, given second reading on December 7 and sent to the Commons Finance Committee for detailed study. It passed third reading without amendment to the sections under consideration here on February 27, 2007. The Senate gave the Bill three readings between February 28 and March 29, 2007, and it received Royal Assent the same day.

Bill C-37 was an omnibus bill containing several hundred sections on a wide variety of topics related to the federally-regulated aspects of the financial services industry. The sections amending the *Bills of Exchange Act* were enacted by section 398 as decimal-denominated provisions following section 163 and immediately preceding Part III of the Act, which governs cheques. This location was selected over an alternative proposal to insert them after section 84, which creates the general duty of holders to present bills for payment. The chosen location was preferred as enabling the provisions to appear as a separate group without interrupting the flow of provisions dealing with conventional methods of presentment. It was also noted that they deal with more issues than simply a new method of presentment. They were not added to Part III, since, as will become evident below, they may affect demand payment instruments other than cheques. It would have been useful for the Bill to have enacted a new subtitle to distinguish the provisions from those in sections 159 to 163 dealing with issues concerning the conflict of laws, but its omission is legally irrelevant in any event.¹⁹

¹⁹ See *Interpretation Act*, R.S.C. 1985, c. I-21, s. 14. The courts may look at a marginal note or heading as an aid to interpreting a legislative provision (see e.g. *Corbett v. Her Majesty the Queen*, [1997] 1 F.C. 386 at 396 (Fed. C.A.)), but that would not appear to be necessary to distinguish the new provisions from those dealing with the conflict of laws.

To my mind, the key provision among the new sections is not section 163.3, which authorizes electronic presentment, but section 163.2, which provides:

An official image of an eligible bill may be dealt with and used for all purposes as though it were the eligible bill.

In other words, digital images of the most common payment instruments are about to take the place of the paper-based originals for all purposes once the originals have been delivered to their payees and deposited for collection with a bank.²⁰ Understanding of the way in which that will be accomplished requires a review of the new provisions, although it should also be appreciated that the full extent of the effects of the new provisions cannot be fully understood until the rules of the CPA implementing them are brought into force.

5. Eligible Bills

Section 163.1 defines the instruments that are subject to the new provisions as “eligible bills.” The definition is very short and simple:

The following definitions apply in this section and sections 163.2 to 163.6 ... “eligible bill” means a bill that is of a class specified by a by-law, a rule or a standard made under the Canadian Payments Act.

The new legal regime to govern truncation and electronic presentment of eligible bills does not rest on the new provisions in the *Bills of Exchange Act* alone; this section, and others discussed below, make it clear that the details of the new regime require the preparation and enactment of subordinate legislation by the CPA. I think that there were two main reasons for delegating the power to determine the scope of application of the new provisions to the CPA in this way: (1) in principle, matters of detail are better dealt with by subordinate legislation, especially where operating conditions may require change from time to time; and (2) the by-laws, rules and standards of the CPA are subject to ministerial oversight. Under the *Canadian Payments Act*,²¹ the by-laws passed by the members and directors of the CPA “are not effective until approved by the Minister [of Finance],”²² and the rules, which must be authorized by by-law,²³ must

²⁰ “Bank” is used here in the expanded sense authorized by s. 164 of the *Bills of Exchange Act*, *supra* note 1 to include all members of the CPA.

²¹ R.S.C. 1985, c. C-21, as amended by S.C. 2001, c. 9, s. 223.

²² *Ibid.*, s. 18(2), as am. by S.C. 2007, c. 6, s. 429(3). The provision was added by Bill C-37, but is not yet in force.

²³ *Ibid.*, s. 19(1) (“Subject to the by-laws, the Board may make such rules ...”).

also be submitted to the Minister for review following passage.²⁴ In addition, the *Canadian Payments Act* enables the Minister to issue both mandatory and prohibitive orders with respect to the content of any by-law, rule or standard of the CPA.²⁵ Hence, there is no loss of governmental control involved in delegating to the CPA the task of defining the scope of application of the new statutory provisions in its rules, from time to time.

The CPA made the first public version of its *Draft TECP Rule*²⁶ available to some interested persons sometime in June 2007, and posted a copy on its Web site²⁷ until the expiration of the public consultation period at the end of August, the same year. Part II of the version of the *Draft TECP Rule* that was posted provided a detailed list of the instruments that are proposed to be eligible for truncation and electronic presentment. It would be inappropriate to comment on the contents of this draft list since it may be subject to extensive change in the process of finalization and ministerial review. It is sufficient to note that, in addition to cheques, the final list will probably designate several forms of paper debit items that are exchanged by member financial institutions at present as a part of the administration of the national debit clearing and settlement system of the CPA. They would comprise such items as settlement vouchers and the miscellaneous inter-member debits that member banks use to collect small sums from each other. It will probably also include several common forms of payment instrument that are not subject to the *Bills of Exchange Act*, such as Receiver-General's warrants,²⁸ some federal and provincial savings bonds, as well as some other forms of coupon and gift certificate debits that are typically not in the form of bills of exchange.

On reflection, it seems highly likely as well that some of the instruments that are routinely truncated will, on professional examination and interpretation, fail to qualify as "cheques" for some technical reason - because they are not unconditional, for example,²⁹ or because they order "any act to be done in addition to the payment of money,"³⁰ or (not being payable to bearer) do not specify the payee with reasonable certainty.³¹

²⁴ *Ibid.*, s. 19(4).

²⁵ *Ibid.*, s. 19.3(1), as enacted by S.C. 2001, c. 9, s. 235.

²⁶ "TECP" is the CPA's acronym for "truncation and electronic cheque presentment;" see Canadian Payments Association, *Draft TECP Rule*, version 6.5, c. 1 at 4.

²⁷ <http://www.cdnpay.ca>.

²⁸ Which cannot qualify as bills of exchange if they are not drawn on a bank, or if the Crown is a party but not a "person;" see Crawford, *Payment, Clearing and Settlement*, *supra* note 11, c. 18 at 2.4(b)ff.

²⁹ *Bills of Exchange Act*, *supra* note 1, ss. 16(1),(3).

³⁰ *Ibid.*, s. 16(2).

³¹ *Ibid.*, s. 20(4).

That could be significant, since only “bills” are eligible to be “eligible bills,” and only “eligible bills” will receive the benefit of the new provisions. On first impression, that may sound rather ominous, but I do not think that it will be a problem in practice because payment items that fail to qualify as bills are almost always found to be governed by the provincial law of contract,³² which typically places virtually no importance upon the continued existence of a paper as a condition precedent to the enforcement of the rights and duties of the parties. Fortunately, a bank that destroys a payment instrument that does not comply with the definition of a bill of exchange would be exposed to a claim for the sum payable as damages for conversion by the instrument’s owner only if the rights of any party were found to have been lost or diminished as a result, which should seldom be the case. I discuss below³³ the probability that provincial electronic documents legislation will complement the federal law and preserve the legal value of the information contained in forms of TECP-eligible items that do not qualify as eligible bills.

For all normal purposes of most persons, therefore, the definitions should probably be taken to mean that all cheques, including certified cheques,³⁴ that they create and receive as payment instruments will be subject to the new procedures and therefore represented only by an official image once they have been deposited for collection by the payee, and destroyed by the collecting bank.

For the CPA and its members, however, there is another issue; a significant number of the cheques that are deposited each day are drawn on the same bank into which they are deposited for collection. This happens each time the drawer and the payee of a payment item bank with the same financial institution. Such items are called “on-us items,” and may be collected and paid by the bank without any inter-bank exchange or settlement or, therefore, any involvement of the CPA or use of its systems and procedures.³⁵ In effect, the bank presents these items to itself for payment and, if they are approved, pays them by making a simple adjustment in its records of the balances in the accounts of the drawer and payee. When the new provisions were being drafted a question arose as to whether the protections they offered could be extended so as to apply to on-us items as well. There was, in addition, a question whether the CPA’s

³² See Crawford, *Payment, Clearing and Settlement*, *supra* note 11 c. 19 at 2.10ff.

³³ See text at section 8, *infra* at 214-17.

³⁴ It may be deduced that certified cheques are included because nothing in either the new statutory provisions or the draft TECP Rule excludes them.

³⁵ The *Canadian Payments Act*, *supra* note 21, limits the objects and powers of the CPA to the exchange and settlement of payment items among members.

statutory powers extend beyond inter-member exchange and settlement, to include on-us items. However, on reflection, it became clear that no issue concerning the limits of CPA's statutory mandate arises. On-us items are not addressed because there is no need to do so. The definitions of "eligible bill" and "official image" are clearly broad enough to include on-us items and there is no need to exempt the bank that is processing the on-us items from the requirements of due physical presentment of the *Bills of Exchange Act*. The eligible bill is in the possession of the drawee bank; the requirement of section 48(3) that the holder "exhibit" the bill and demand payment is satisfied when the payee or other holder delivers the item to the drawee for deposit. For all other purposes on-us items may be eligible bills and may be converted to official images with the same legal consequences as for all other forms of eligible bills.

6. Official Images

Section 163.1 of the *Bills of Exchange Act* now provides the following definition of "official image:"

"official image," in respect of an eligible bill, means an image of that bill created by or on behalf of a bank in accordance with by-laws, rules or standards made under the Canadian Payments Act, together with any data in relation to the eligible bill prepared in accordance with those by-laws, rules and standards, and includes a display, a printout, a copy or any other output of that image and that data created by or on behalf of a bank in accordance with those by-laws, rules and standards.³⁶

There are two important points to note about this definition. The first is that the official image includes any data relating to the eligible bill that the final version of the TECP Rule of the CPA will provide for, and that the collecting bank transmits along with the digital image of the item itself. This may call for a word of explanation for those not familiar with payments systems operations. It is anticipated that, for ease of operation of the system, the cheque-processing centre of the collecting bank (or its clearing agent or other representative) will prepare a brief summary of the key features of each eligible bill that it processes for truncation. In the case of a common cheque, this would probably include only the number of the cheque, the date, the sum payable and the encoded information identifying the branch and account on which it is drawn. This summary will be transmitted to the drawee bank along with the digital official image, and will be the basis on which the drawee gives credit to the collecting bank in provisional settlement for the instrument in the national debit clearing system. Each bank, however, will probably establish its own new criteria

³⁶ "Image" is defined in draft TECP Rule, Part I, s. 4 as "a digital representation of the front and back of a TECP-eligible item...."

to determine which actual images of truncated cheques will be examined by personnel at the branch of account before the cheques are considered to be finally paid and charged to the drawer's account. That is because only the part of the official image that actually replicates the face and back of the eligible bill will disclose the information that the staff will require in order to confirm the signature of the drawer and to check for any necessary endorsements. Banks are free to make a business decision as to how much scrutiny to give to a cheque before paying it. The inclusion of the accompanying data in the definition of "official image," therefore, necessarily justifies the banks' use of both the summary and the digital replica of the eligible bill for the purposes for which each is appropriate.

It should also be noted that there may be more than one official image of an eligible bill, and they may not necessarily be identical in all respects. When an eligible bill is first deposited with a bank for collection, it will be transformed into an official image that will show the face and back of the instrument, together with any signatures and bank stamps that are on it at that time. The collecting bank will transmit a file containing that official image and, as noted above, a summary of other data relating to it, which will assist the drawee bank in identifying it and processing it quickly. The collecting bank will retain that original file, with or without the addition of any new information that it may add for the purposes of its own internal processing and archival purposes, and reporting to its customer. Those processes produce, therefore, at least two files containing official images and related data that are not identical. An official image that is provided to the drawer with a monthly account statement will probably not contain any of those additional data, nor will those data be appended to any certified form of official image provided in paper form at the request of the customer or other interested person. Other electronic files may also be created without the accompanying data if the customer receives and archives periodic reports from its bank in electronic form. Again, if an official image is not paid by the drawee bank because the funds on deposit in the drawer's account are not sufficient to pay it, or because the account is closed, the image re-transmitted by the drawee to the collecting bank will have more data attached than were contained in the file originally presented. Files passing through the facilities of clearing agents or other representatives of indirect members of the clearing organization will similarly carry some electronically recorded evidence of their routing and processing. Such annotations are essential for the efficient operation of a bulk clearing and settlement system, and should not cause any more difficulties for lawyers or courts than the stamps that now record on the backs of cheques the same information as to details of their passage through the inter-bank systems, whether the additional data are recorded in

an accompanying file, or actually added to the official image of the front or back of the eligible bill.

I discuss below³⁷ the provision discharging all official images of each eligible bill once one such image has been paid.

7. Presumptions Supporting Official Images

Two very important provisions create rebuttable presumptions of authenticity and accuracy of official images:

163.4(1) In the absence of evidence to the contrary, a document purporting to be an official image of an eligible bill is presumed to be an official image of an eligible bill...[and]

(3) In the absence of evidence to the contrary, an official image of an eligible bill is presumed to be a true and exact copy of the eligible bill.

In addition, the bank that transforms an eligible bill into an official image impliedly gives a statutory warranty that the official image was created in accordance with by-laws, rules or standards made under the *Canadian Payments Act*, and that it accurately represents the eligible bill.³⁸

In simple terms, therefore, an official image, whether in electronic form as a file or screen, or in physical form as a document, may be accepted by all persons as an authentic and accurate representation of the eligible bill that it purports to represent and/or to re-embodify. It is anticipated that each official image will contain some simple form of assertion that it is an official image, so as to distinguish it from an informal, insecure and possibly fraudulently altered photocopy of the original, which might be created by anyone.³⁹ However, an actual certificate of authenticity issued by the collecting bank (or its agent or other representative for the purpose of truncating the instrument) that first received the original eligible bill for deposit and collection may be provided only upon request. That would appear to make it necessary for interested persons to contact the truncating financial institution if some question were to arise as to the accuracy or completeness of an official image, or a challenged copy purporting to be an official image. That, in turn, will require the truncating financial institution to include, as part of each official image, some form of identifying stamp or mark bearing its

³⁷ See s. 163.3(2) in section 8(D), *infra* at 223.

³⁸ See s. 163.6(1) in section 9, *infra* at 223.

³⁹ Note that s. 163.4(1) of the *Bills of Exchange Act*, *supra* note 1 requires that an official image “purport” to be such, which I understand will require some form of assertion in the text of the image file itself.

name and address, and a sequence or serial number to enable the item to be identified. The new provisions do not address the issue as to whether that institution may charge a fee for such a service, but in view of the huge cost savings to industry participants that truncation and electronic presentment will produce, there would appear to be no justification for a fee in the few cases in which certified copies of official images may be required.

8. Legal Equivalence

The following provisions of the Act address the issue of legal equivalency:

163.2 An official image of an eligible bill may be dealt with and used for all purposes as though it were the eligible bill.

163.5 If an eligible bill is destroyed ... and there is an official image of the bill ... :
(b) the destruction does not affect any person's rights, powers, duties and liabilities in relation to the eligible bill ...

The new sections of the *Bills of Exchange Act* attempt to ensure that official images are the legal equivalents, for all purposes, of the eligible bills from which they were created. Legal equivalence was perceived on all sides as a necessary condition of the move from paper cheques to digital images. That is, if electronic presentment was the reason that the CPA sought the legislative authority to truncate, legal equivalence was the *quid pro quo*, perceived on all sides as being necessary in order to ensure that the new banking procedures do not accidentally create any new problems for members of the public.

“Legal equivalent” is convenient shorthand for the latter concept, but the section does not use the expression, which is found, for example, in the American *Check 21 Act*.⁴⁰ Even the sidenote of the Canadian section refers only to the “status of official image.” A concern was that “legal equivalent” had no established meaning in Canadian law and would, therefore, require definition if it was to be used. The more simple and direct solution was to provide expressly for the desired legal effect of the definition while avoiding the term. That approach is similar to that adopted by the Uniform Law Conference of Canada in its *Uniform Electronic Commerce Act*,⁴¹ and enacted by all the common law provinces and two territories. For example, the Ontario version of that template provides:

⁴⁰ U.S., Bill H.R. 100, *Check Clearing for the 21st Century Act*, 108th Cong., (2003), s. 4(b) (enacted) (“A substitute check shall be the legal equivalent of the original check for all purposes ... and for all persons ...”).

⁴¹ See e.g. Uniform Law Conference of Canada, *Uniform Electronic Commerce Act* (1999), online: < <http://www.ulcc.ca/en/us/index.cfm?sec=1&sub=1u2>> (“Information shall not be denied legal effect or enforceability solely by reason that it in electronic form”).

Legal recognition of electronic information and documents 4. Information or a document to which this Act applies is not invalid or unenforceable by reason only of being in electronic form.⁴²

Legal recognition of the continued value of the information in an original document, despite its transformation to electronic media, seems to me to be very like validating the legal effects of all dealings with and uses of the information in a cheque or other eligible bill despite its transformation to an official image. At the same time, it should be noted that to copy the precise formulation of the precedent idea would have been inappropriate in the context of the *Bills of Exchange Act*. The provincial law, in addition to continuing the validity and enforceability of the information in documents that are converted from paper to electronic form, validates information that is in electronic form from the time of its creation. That was further than Parliament was asked to go in connection with cheques. It was also thought to be necessary in the context of the transformation of eligible bills to official images for the new provisions to provide expressly for the continued validity and enforceability, not only of the contracts and other rights and duties of the parties to the eligible bill, but also of the property rights that parties had in the paper originals – and all this despite the destruction of the original. In the light of the historical importance and continued statutory requirement of possession of a negotiable instrument as a condition precedent to enforcement, it would not have been enough for the new sections of the Act merely to provide that “the information” representing those rights and duties did not become invalid or unenforceable by reason of the creation of the official image: the new provisions had to provide that the official image re-iterated them to the same extent and effect that the eligible bill had done. In my opinion, the new provisions achieve this goal.

In accordance with the literal and intended meaning of section 163.2, a person who wishes to deal with or to use a cheque for any purpose may deal with or use the official image in the same ways except, of course, for the purpose of further negotiation or transfer, discussed below. That should be sufficient for all foreseeable purposes. For example, if the official image is of a genuine eligible bill,⁴³ the drawee bank will be fully justified in settling for it and debiting the drawer’s account. A person wishing to prove that they made a challenged payment should now, either routinely or upon specific request, provide a photocopy of the official image that their bank

⁴² *Electronic Commerce Act*, S.O. 2000, c. 17, s. 4.

⁴³ If what purports to be an eligible bill is a forgery or subject to some defect that prevents the holder or the collecting bank from acquiring the right to payment, the official image will be similarly flawed and will not protect the drawee bank from liability for wrongful payment.

will give them. Furthermore, if a copy of a cheque is required for the purposes of giving notice of dishonour or recording an official protest for some special purpose, the official image will fulfill all legal requirements as a substitute for the original, whether or not that original has been destroyed at the material time. Other uses of section 163.2 and of official images as fully competent substitutes for the original eligible bills may easily be imagined.

It should be noted, however, that only *legal* equivalence may be addressed in legislation. Full practical equivalence for all purposes is not achievable. Plainly, as a practical matter, an official image is not an identical clone of the eligible bill from which it is produced, even if no iota of the information represented in the eligible bill is omitted or distorted by the transformation into an image. Experts whose opinions are sometimes used to validate signatures or whole documents for the purposes of trying criminal charges of forgery, for example, will no longer be able to analyze the paper and ink of a challenged document as part of their investigations. Other subtle differences between an eligible bill and an official image of it may also be lost. I understand, for instance, that the same experts find that their studies of challenged signatures and other writings are more reliable when they include analysis of the variations in the pressure by which the penned portions were applied to the original paper. Apparently even the most sophisticated equipment now available to transform an eligible bill to an official image cannot replicate the effects of those variations in pen pressure, and some present uses of eligible bills may be lost in the transformation to official images. It seems that technology giveth, and technology taketh away – for the present, at least.

An official image is the legal equivalent of the original eligible bill; it is not the eligible bill, or even a bill in and of itself. Although there will be multiple official images, the only official image that the drawee bank will honour by payment is the first one that it receives from the collecting bank (or its clearing agent or other representative) through the cheque clearing and settlement facilities of the CPA. Since all official images are discharged by that payment,⁴⁴ there would appear to be little incentive for anyone to forge or fraudulently alter a paper-based official image, at least for the purpose of appropriating the sum payable. An official image would not be paid if presented for payment at the counters of the drawee, for example, or qualify as a cheque for any other purpose (since it would bear only a replica of the drawer's signature) and is not made a negotiable instrument by the new provisions of the Act. No one should accept an official image as a payment item, whether or not it is endorsed by anyone

⁴⁴ See discussion of s. 163.3(2) in section 8(D), *infra* at 223.

except, of course, the drawee bank that receives it through the clearing and settlement facilities of the CPA.

The new provisions do not rely entirely upon general statements of principle to ensure legal equivalence: they go on to specify legal equivalence in four important contexts: electronic presentment; preservation of rights; admissibility in evidence; and discharge by payment.

A) Electronic Presentment

Section 163.3(1) of the *Bills of Exchange Act* reads as follows:

Despite anything in this Act, a bank may present for payment an official image of an eligible bill electronically in accordance with by-laws, rules and standards made under the Canadian Payments Act and, if it does so, the requirements of this Act respecting the presentment for payment of the eligible bill are deemed to have been complied with.

This provision addresses one of the chief concerns with earlier truncation proposals by permitting banks to satisfy in a new way the old statutory requirement that presentment requires that the holder “exhibit the bill” to the person from whom payment is demanded.⁴⁵ As such, it takes the same approach as, and effectively duplicates, the existing section 29 of the *Canadian Payments Act*.⁴⁶ That is the section that has, since 1982, permitted members of the CPA to present cheques and other eligible payment items by means of inter-bank exchanges of items in bulk at special clearing centres, rather than individually at the branch of account, as a literal interpretation of the *Bills of Exchange Act* would otherwise require. While duplicative legislative provisions are undesirable in principle, in this case the benefit of having two sections was apparent, for two reasons. As it stands, section 29 could have been considered to be inadequate to the task of covering all the technical objections to truncation that could be raised with respect to the proposed scheme, particularly as many of the incidents of the scheme will clearly impinge on the rights of the public, and on issues far removed from the technicalities of clearing house operation and the duties of collecting agents. It is also a provision with which most lawyers are unfamiliar. While it would have been possible to amend section 29 to add the necessary new material, it is preferable to put the new provisions where they will most easily be found. The *Bills of Exchange Act* is a familiar source of law governing cheques; the *Canadian Payments Act* is not. At the same time, it is not possible to repeal section

⁴⁵ See text at section 2, *supra* at 204.

⁴⁶ The section reads: “Members may present payment items ... in accordance with the by-laws and the rules.”

29, since it has broad application to many more forms or types of payment items than merely cheques and the other types of “eligible bills.” Section 163.3(1) provides a viable solution, despite the undesirable element of duplication, by supplementing the provisions of section 29.

I say that the new provision supplements section 29 because it effectively discharges the collecting bank from all residual liability to present an eligible bill physically in the event that some failure, mistake or omission in the processes of the collecting or drawee banks results in the loss of the item, or in loss of rights through delay. Section 29 permits a collecting bank to send an item to the drawee bank through the facilities of the CPA as an alternative to conventional presentment for payment by promptly “exhibiting” each bill to its drawee at the place designated for payment in it. If some disruption of the CPA’s facilities were to prevent their use for a time, the *Bills of Exchange Act* duty to present promptly would remain. Section 163.3 goes further by deeming the collecting bank to have complied with its statutory duties if it complies with the CPA’s rules for electronic presentment. Presumably those rules will address the possibility of a failure in the systems of both the collecting and drawee banks, as well as the CPA’s own systems, and make provision for alternative methods of presentment or for permissible delays while normal operating conditions are being restored. Compliance with those contingency rules will also be deemed as compliance by the collecting bank with the statutory duties. This distinction could have important practical consequences if, for example, the CPA’s system is out of commission for a significant time, or if an original bill has already been destroyed before a problem with its presentment is discovered.

B) Preservation of Rights

A second section of the new provisions seeks to eliminate several technical difficulties that could have arisen under the pre-Bill C-37 law by reason of the fact that all eligible bills will be fairly promptly destroyed as part of the new process. Section 165.3 states:

- If an eligible bill is destroyed in accordance with by-laws, rules or standards made under the Canadian Payments Act and there is an official image of the bill:
- (a) a person’s rights and powers in relation to the eligible bill are not affected by reason only that the person does not possess it;
 - (b) the destruction does not affect any person’s rights, powers, duties and liabilities in relation to the eligible bill; and
 - (c) the eligible bill is not considered to be lost or to have been materially altered or intentionally cancelled.

Not much comment is required to elucidate the clear intent and effect of those provisions. Possession of the original eligible bill, essential to the enforcement of holder's rights for more than two centuries, is now unnecessary. Destruction of the original eligible bill has no effect on the legal position of any party to it, or any member of the CPA that actually destroys it.⁴⁷ The eligible bill is not to be considered to have been lost, or materially altered, or intentionally cancelled – all grounds for discharge of the primary party under specific sections of the *Bills of Exchange Act*⁴⁸ and the old law interpreting them.

But it should be noted that the section refers only to rights and powers “in relation to the original bill” being preserved. That may not translate into perfect equivalence with the rights of the holder of the official image. For example, if the actions of a person with respect to an eligible bill, while it remains in tangible form, amount to a conversion of it, the rightful owner's claim would continue despite the transformation of the bill to an image. What is not clear from the new provision, however, is whether actions performed on, or only with respect, to the official image that would have amounted to a conversion of the eligible bill if they had been performed on or with respect to it, will still provide the rightful owner with all the same remedies they would have had if only the original had been dealt with. In other words, if a bank collects a cheque for a person who is not entitled to it, the bank will remain liable in conversion, despite the transformation of the cheque into an official image. On the other hand, if a drawee bank wrongfully pays an official image that is not properly payable by its customer, it is not clear that it converts the official image. The bank will be liable in damages for the amount of the wrongful payment but, perhaps, because of its breach of its contract; not on a theory of conversion of either the cheque or the official image. The difference could be significant in cases in which some contributory negligence or fault is attributable to the customer. Contributory negligence is not a defence to an action for conversion.

I might just add that there is no need for section 163.5 to negate the possibility of the destruction of an eligible bill being interpreted as a renunciation of a holder's rights under section 141 of the Act. Subsection 141(3) makes it clear that renunciation requires a separate writing unless

⁴⁷ S. 430(1) of Bill C-37, now S.C. 2007, c. 6; s. 430(1) added paragraph (b.1) to the powers of the Board of the CPA to make rules for the national cheque-collection system under *Canadian Payments Act*, *supra*, note 13, s. 19(1): “(b.1) respecting the destruction of payment items.” Destruction of an item under the authority of a rule sanctioned by federal law could not conceivably be a conversion of the item, or any other kind of actionable wrong.

⁴⁸ See text at section 2, *supra* at 204.

the bill is delivered to the acceptor. The process of truncating eligible bills for electronic presentment as official images will not give rise to either possibility.

The *Electronic Commerce Act* of a province may function as a complement to the new federal “official image” provisions of the *Bills of Exchange Act* by preserving the rights of persons to instruments that are truncated but not within the scope of the protection given by the federal law. Banks may truncate all instruments that appear to satisfy the criteria of TECP-eligible items without giving much thought to whether or not they technically qualify as eligible bills. If the items do qualify, then both the contractual and proprietary rights of all parties are preserved by the new provisions of the federal law. If they do not qualify for federal protection, at least the *contractual* rights of the parties are expressly protected by the applicable provincial *Electronic Commerce Act*. Only in the exceptional case would those rights not be sufficient to save a party from loss by the accidental truncation of an ineligible bill or payment instrument and the resulting loss of *proprietary* rights in it. In those rare cases, the injured party would appear to have a claim against the truncating bank for damages for conversion or breach of the statutory warranty, provided that the lost rights can be shown to have been of some value not represented by the contracts of the parties.

C) Admissibility in Evidence

Section 163.4(2) of the Act reads:

An official image of an eligible bill is admissible in evidence for all purposes for which the eligible bill would be admitted as evidence, without proof that the official image was created by or on behalf of a bank in accordance with the by-laws, rules or standards made under the Canadian Payments Act.

The clear intent of this provision is to make it unnecessary in the ordinary case for a court to examine any foundation evidence by affidavits or *viva voce* testimony of bankers or information technology support staff, concerning the equipment, programs, procedures and business practices that produced the official image. If the eligible bill would have been admissible, so is the official image. The eligible bill is no longer the “best evidence” of its contents or condition; the official image is. In the absence of evidence to the contrary, a document purporting to be the official image is presumed to be the official image,⁴⁹ and is presumed to be a true and exact copy of the contents of the eligible bill.⁵⁰ Of course, in an

⁴⁹ *Supra* note 1, s. 163.4(1).

⁵⁰ *Supra* note 1, s. 163.4(3).

exceptional case where the accuracy of an official image is challenged by a party, and there is conflicting evidence as to the actual contents or form of the eligible bill, the court may have no alternative other than to delve into the conflicting material and to decide which account is the more reliable. The new provisions do not address that possibility, other than to leave it open. In such an inquiry, all the ordinary laws of evidence and fact-finding will apply.

At the level of administrative procedure, the effect of the new provisions on the traditional insistence of many federal and provincial ministries and agencies on the submission of originals of cancelled cheques and other payment instruments is a little indirect. The Act does not mandate, for example, that every government department and agency change its rules and guidelines regarding the acceptability of copies of cancelled cheques. The obligation of a governmental agency of any description and at any level to accept official images may, however, be deduced from the provision in section 163.2 that an official image “may be dealt with and used for all purposes as though it were the eligible bill.” When fully implemented by approved rules of the CPA, the existence of that new provision will require that all persons review, and possibly revise, some existing evidentiary policies and practices that pre-date the passage of Bill C-37.

The policy underlying the new statutory provision is clear. Until Bill C-37, the conversion of business records into electronic files was almost always done for the convenience of the business whose records were involved. Official images of eligible bills are different. Parliament has approved the government’s announced policy⁵¹ of reducing the costs and increasing the efficiency of the national cheque collection system by authorizing a total shift to official images. Currently, that system processes millions of individual items each day, billions each year. It would be simply too onerous for both customers and banks if the law were to continue to permit creditors or others to demand foundation evidence of some bank’s cheque truncation operations from each person who tenders an official image as proof of payment in future. Every time a dispute arose in which a person sought to table an official image of their cheque, an affidavit or other evidence from a banker would be required to establish the regularity of the process by which it was created. That would be impractical and an unwarranted intrusion on the rights of the public. If a technical foundation for abandoning the old rules is required it might be found in a new application of the presumption of regularity, which accepts

⁵¹ Recall the statement by Hon. Jim Flaherty, Minister of Finance, quoted at the beginning of this comment.

that very common business practices are routinely followed in the required manner.⁵²

D) Discharge by Payment

Section 163.3(2) of the Act states:

The eligible bill and its official image are discharged if payment in due course is made by or on behalf of the drawee after the electronic presentment for payment of the official image of the eligible bill.

In view of the fact that there may be multiple computer-based files containing versions of an official image, as I tried to explain above,⁵³ a question may arise whether this section intends to discharge all official images of an eligible bill upon the discharge by payment of any one of them. The risk that a second or third version of an official image might be presented for payment through the facilities of the CPA at some later time is a practical possibility, either as a result of error or system malfunction. Clearly, it would be desirable for the subsection to be interpreted as exonerating the drawee or other primary party from any such second or additional liability. Such an interpretation might be supported by the logic of the new provisions, taken as a whole, perhaps supplemented by reference to subsection 33(2) of the *Interpretation Act*.⁵⁴

9. Warranty and Damages Liability of Bank

As a final safeguard of the rights of the public, the new provisions provide recourse to the truncating bank:

163.6(1) A bank that creates or purports to create an official image of an eligible bill, or on whose behalf an official image of an eligible bill is created or purported to be created, warrants that the official image or purported official image, as the case may be, was created in accordance with by-laws, rules or standards made under the Canadian Payments Act and that it accurately represents the eligible bill.
(2) Any person who has suffered damages as a result of a breach of the warranty has a cause of action for damages against the bank.

⁵² See e.g. John Sopinka, Sidney N. Lederman and Alan W. Bryant, *The Law of Evidence in Canada*, 2d ed. (Toronto: Butterworths, 1999) c. 4 at 52-53ff, citing English authority applying the presumption (in the absence of any evidence either way) to decide that the traffic lights installed by municipal authorities were operating correctly at a material time.

⁵³ See text at section 2, *supra* at 204.

⁵⁴ R.S.C. 1985, c. I-21, s. 33(2): "Words in the singular include the plural"

The policy supporting this new statutory right has already been adverted to, and may be fairly simply restated. While it is probably true that almost everyone will benefit in intangible ways from the anticipated increase in the efficiency and speed of the new cheque collection procedures, it is also true that the most easily quantifiable benefits will be realized in the form of cost savings by the depository financial institutions that are members of the CPA. At the same time, since the items to be destroyed are the property of the institutions' customers,⁵⁵ any risk of malfunction of the system, or any unforeseen loss of rights as a result of truncation, will probably fall on them. The statutory right to damages attempts to redress that imbalance of the incidence of the benefits and costs by providing for compensation.

Since an official image will be paid only if presented by a member of the CPA through the established national cheque-collection system, there is no practical possibility that criminal or fraudulent persons might be able to use forgeries of official images to obtain money. The warranting bank can never therefore be liable in damages for diverting the sum payable on an official image, unless it would have been liable if it had similarly diverted the sum payable by the eligible bill instead. Nor, on reflection, is there any practical possibility that section 163.6(1) could be misinterpreted to impose liability on a warranting bank for some other use of a complete fabrication or forgery of an official image, where no corresponding eligible bill had ever been in the possession of the bank. While a forgery of an official image might, and probably would, "purport" to be legitimate, the conditions precedent of the statutory warranty are fulfilled only when the eligible bill that was transformed into the official image that has caused someone loss or damage was actually in the possession or under the control of the warranting bank, or by someone acting on its behalf.

This reference to persons acting as representatives or otherwise "on behalf of" a member bank may require brief explanation for clarity. For the past ten years, or so, many of the cheque-processing and data-processing facilities that support the national debit-clearing system in Canada have been owned and operated not by the individual banks, but by larger or more senior banks, or by separate corporations formed by consortia of participating banks, or by independent specialist data-processing enterprises. These entities perform cheque-processing services for their customers. Their duties are provided for in the agreements they have with their customers. They have no rights or official status in the CPA's system; only their customers remain primarily liable for any errors, omissions, losses or damages that their negligent operations may cause to members of the public whose payment items are processed by them. It is anticipated

⁵⁵ Whether as payees, other holders or, by default, drawers of the instruments.

that these outsourcing arrangements will continue and, therefore, the section addresses the possibility that a particular official image might have been produced by one of those other participants, rather than by the collecting bank itself. I think that the section accomplishes that objective with the words “or on whose behalf etc.” without creating any new liability on the service providers or their principals. The section may also prove useful in future to support cheque imaging by major creditors, such as public utilities.

Finally, I wish to note that the section does not mandate a payment of damages by the truncating bank to the person damaged by the conversion of an eligible bill into an official image. It creates the cause of action, but leaves the issues of causation, foreseeability and the measure of recoverable damages at large, to be dealt with by the courts. In other words, I think that “cause of action” is not used in the technical sense in which it sometimes appears, that is, to describe “the facts on which the plaintiff relies to establish a claim.”⁵⁶ In the context of the new provisions to the *Bills of Exchange Act*, the reference to the *cause* of action may be better understood as creating a *right* of action or, perhaps, a statutory duty upon the truncating bank to ensure that no harm befalls any member of the public - or indeed any person - by this shift from paper cheques and other eligible bills to digital images of them. The damage may be suffered by the drawee bank, if for example the change to a digital image can be shown to have actually misled it as to the validity of the signature on the converted instrument. Or the damage may be suffered by the drawer of the eligible bill, if the process of transforming an eligible bill into an official image and summary somehow changes a material part of the original, such as the sum payable, or the date of the payment order, or if a collecting bank’s system mistakenly presents and receives payment of the digital image more than once. Or the damage may be suffered by the payee if the truncation and electronic presentment process loses the eligible bill or the official image, or accidentally destroys an eligible bill before an official image can be created. In all of such cases, and in others that will probably arise, the claimant will have to show the facts proving, on a balance of probabilities, that the process of truncation caused loss or damage in an ascertainable amount. It will not be necessary to show that the system malfunctioned; if damages are proven to have resulted as a result of the operation of the truncation scheme, it will not matter whether that was due to an accident, or the result of an unforeseen consequence of the proper operation of the system in accordance with its design.

⁵⁶ See *Letang v. Cooper*, [1965] 1 Q.B. 232 at 242-3 (C.A.), Diplock L.J.: “A cause of action is simply a factual situation the existence of which entitles one person to obtain from the court a remedy against another person.”

I think that ordinary principles of foreseeability will apply to determine the appropriate measure of recovery. I cannot conceive of a reason why they should not. If a cheque in payment for shoes for the French army is not paid, and the sale is lost accordingly, the recoverable damages ought still to be measured with reference to the sum payable by the cheque, not the anticipated profit on the sale!⁵⁷

The measure of damages may well vary with the circumstances of the claim. Damages for conversion of an eligible bill or official image⁵⁸ need not be the same as those for wrongful dishonour of an official image. The courts will have to work out the details. All that the new section does is to put beyond argument that the claimant has a right of action, and cannot be turned back at the threshold.

10. Conclusion

The new provisions added to the *Bills of Exchange Act* to authorize the conversion of cheques and other eligible bills, and the destruction of the originals, will produce some dramatic changes in the ways in which cheques are processed and payments are proved. If the new provisions are given their literal meaning and clear intent, those changes will not result in any change in the legal rights or duties of any person. If someone does show that they were damaged in some measurable and foreseeable way by the destruction of the eligible bill or the new method of processing, they have a right of action to recover compensatory damages from the bank that performed the conversion.

⁵⁷ With apologies to Alderson B., and the other members of the Court in *Hadley v. Baxendale & Co.* (1854), 9 Exch. 341, 156 E.R. 145.

⁵⁸ It is not entirely clear to me whether it will be possible to claim conversion of an official image. It may be that images lack both that element of exclusive right to immediate possession that characterizes eligible bills and other negotiable instruments, and also any vestige of the quality of “property,” which the claimant must have and which must be materially prejudiced in some way as an essential element of the tort. On the other hand, if a drawee bank wrongfully pays some person other than the rightful owner of the eligible bill it represents, and a claim for damages for breach of contract will not do justice in the circumstances there may be no other satisfactory legal basis on which to award damages. In such an action, the official image could, I suppose, be said to be being “used” for a purpose that would otherwise have been fulfilled by action for conversion of the eligible bill, and all “uses” of eligible bills are continued and extended to their official images by s. 163.2.