

31 March 2015

Senior Adviser  
Financial System and Services Division  
The Treasury  
Langton Crescent  
PARKES ACT 2600

Email: [fsi@treasury.gov.au](mailto:fsi@treasury.gov.au)

Dear Sir / Madam,

### **Financial System Inquiry Final Report**

I am writing on behalf of the Australian Payments Clearing Association (APCA), the self-regulatory body for Australian payments, in relation to the Financial System Inquiry (FSI) Final Report. APCA has been an active participant throughout the FSI and in December 2014, we wrote to Treasury expressing early interest in being involved in the Innovation Collaboration (Recommendation 14).

APCA is the industry association and self-regulatory body for Australian payments and has nearly 100 members. The views expressed herein represent the policy position of the APCA Board as appointed by its members. The views do not necessarily represent the individual views of members.

In our previous submissions to the FSI, APCA identified three principles for payments regulation notably that the FSI should consider:

- a) reaffirming the principle of functional equivalence, first articulated in the Wallis Report;
- b) recognising and supporting co-regulatory responses to emerging challenges in the payments system; and
- c) that government work with industry and other stakeholders to actively promote the use of electronic payments.

We believe that the FSI Final Report, in some areas, reflects these principles – in particular:

- the need for technology neutrality in regulation; and
- for enhanced Government–industry dialogue on issues such as innovation, digital identity and cyber security.

Conversely we note that the FSI Final Report has not indicated support for a co-regulatory approach to emerging payments issues but has rather advocated reformed public regulation through “clearer

graduated payments regulation". APCA believes that, particularly in the context of highly networked payment services, both public and self-regulation have important and complementary roles to play.

Further, the FSI Final Report has recommended a new and untested approach to surcharging for credit card payments and that the Payments System Board (PSB) consider maintaining and refining interchange fee regulation. APCA believes that promoting competition between schemes remains preferable to direct regulation of interchange fees and will consult actively with the RBA on the issues of interchange fees and surcharging.

The Recommendations from APCA's second submission are included as an appendix to this letter.

We wish to comment in more detail on the following issues, commencing with FSI Final Report Recommendations that diverge from APCA's recommendations.

### **Clearer graduated payments regulation – Recommendation 16**

APCA has previously noted that aspects of payments regulation are complex and could be improved. This has been taken up within the FSI Final Report, and there are aspects of Recommendation 16 that APCA would support, in particular extending the ePayments Code to a wider range of entities (though "all service providers" requires careful consideration), publication of a clear guide that outlines thresholds and regulatory requirements and reviewing definitions in the *Payment Systems (Regulation) Act 1998* to clarify the treatment of digital currencies.

APCA's interest in the regulation of payments lies in maintaining confidence in, and the efficiency and security of, the payments system. The proposed changes to the thresholds on non-cash payment facilities requiring an Australian Financial Services Licence (AFSL) are welcomed as providing certainty, as long as the changes do not dramatically shift who is regulated, which could erode existing consumer protections, nor introduce unnecessary risks.

The proposed "two-tiered" approach to purchased payment facilities (PPFs) appears aimed at making it easier for entities to become PPFs. It remains unclear whether the current requirements are acting as a barrier and whether altering the liquidity requirements will in any way encourage more entities to become regulated. Liquidity requirements are critical for ensuring business and consumer users can access and make effective use of value. If denied this, confidence in the overall system is likely harmed. Any reform of the liquidity requirements for PPFs should be carefully considered and remain broadly equivalent to those that ADIs are currently subject to.

While reforming the AFSL and PPF regimes may inject some degree of certainty and flexibility, both of these reforms remain targeted at entities that hold value. The payments world is changing rapidly. Increasingly, new entrants are facilitating the transmission of value and data and not necessarily holding value. These providers often remain outside of the regulatory regime, though a reformed ePayments Code holds out the possibility of bringing them within public regulation.

While technology enables new forms of transacting, it can also put consumer's data at risk. The ADI holding the value can wear liability or be expected to accept risks when consumers use these new methods. Ideally, minimum standards should apply and bodies such as APCA can bring together

stakeholders to identify mutually agreeable outcomes. If done with care, the proposed extension of the ePayments Code may be a key element in ensuring the effective regulation of new entrants.

On this basis, we would support the exploration of targeted co-regulation based on management of consumer risks and careful attention to system integrity, having regard to the networked nature of payments activity.

## **Interchange fees and customer surcharging – Recommendation 17**

### ***Customer Surcharging***

APCA acknowledges that excessive customer surcharging remains a controversial practice that requires close attention. However, it appears that market power exerted by merchants is often the key determinant of excessive surcharging. APCA's existing policy position is that market and self-regulatory based solutions or existing legislation should be explored before consideration of any new price capping response to address excessive surcharging.

The three-tiered approach that the FSI Final Report proposes appears complex and potentially difficult to implement. We are not aware of this approach being implemented or considered anywhere in the world. In particular, we would be concerned if issuers or acquirers were expected to change their practices, for instance whether issuers would be expected to reissue cards so that the card informed the customer whether a system was "low/medium/high". Further, while the PSB would be expected to "set limits" on surcharging, to date this has not been the challenge. Rather the challenge has been in monitoring and enforcement.

The commencement of the RBA's "Review of Card Payments Regulation" on 4 March 2015 provides an opportunity for a more considered and focussed examination of the surcharging issue in close consultation with key stakeholders.

### ***Interchange Fee Regulation***

Interchange fees are a means of rebalancing market prices across two-sided markets. Interchange fee regulation therefore represents a significant intervention into the operation of the market. Since 2000, payment card scheme regulation and economics have been subject to extensive theoretical and empirical study as well as markedly different regulatory approaches in many countries. There is nothing approaching a clear consensus on the optimal regulatory approach.

As previously stated in RBA-convened policy reviews and to the FSI, APCA believes promoting competition is generally preferred to regulation. APCA is disappointed that the FSI Final Report, as an inquiry with a long-term perspective, has not reflected upon the long-term sustainability of this regulatory intervention, particularly as technology and competition in payment services evolve. Further, the FSI Final Report appears to primarily credit interchange fee caps for creating and maintaining efficient payments in Australia – while other factors such as technological innovation and industry initiatives surprisingly receive no mention.

The FSI Final Report suggests the matter of interchange fees remain with the Payments System Board. APCA broadly endorses this and will engage with the RBA through the “Review of Card Payments Regulation” process on issues of interchange fees and surcharging.

## **Other Issues**

### **Collaboration to enable innovation – Recommendation 14**

We have previously indicated that if the Government proceeds with the Innovation Collaboration, that APCA can bring its insight and experience to help such an initiative succeed. APCA has a strong track record of working with industry participants and key stakeholders to identify and develop collaborative initiatives that are beneficial to industry, the financial system and the wider community.

### **Digital identity – Recommendation 15**

APCA believes that digital identity remains an important issue for both industry and Government. APCA supports the exploration of a national digital identity strategy and suggests that the Australian Payments Council and APCA are well placed to help develop industry-wide views on digital identity that balance security concerns with need for competition, innovation and efficiency, and the need to promote security and trust for the consumer.

### **Data access and use – Recommendation 19**

While data access and use were not issues canvassed at length in our previous submissions to the FSI, APCA is supportive of further investigation in the improved use of data and, depending on the specific terms of reference, would consider being involved in any future Productivity Commission review of this issue.

### **Strengthen the focus on competition in the financial system – Recommendation 30**

The periodic review of regulators in respect to competition should focus on outcomes for users of financial services and payments systems. In undertaking these reviews, competition should be assessed alongside innovation, investment and the regulatory framework to identify how to achieve the best outcome for users.

### **Compliance costs and policy processes – Recommendation 31**

APCA broadly supports adequate time being given to implement complex regulatory change and for the undertaking of post-implementation reviews of major regulatory changes. Where possible, these reviews should be done by an independent body rather than the responsible regulator themselves.

### **Cyber security – Recommendation 38**

APCA supports industry and government coordination on cyber security and sees value in, and would like to be involved with, strategic work on this issue. APCA notes it is important to avoid unnecessary overlap in undertaking any such strategic work. The Australian Payments Council also has an interest in cyber security and will be registering its own interest in the issue.

### **Technology Neutrality – Recommendation 39**

APCA is supportive of regulation being technology neutral and has recommended preparation of an omnibus bill by the Attorney-General's Department to remove specific references to cheques in Federal legislation. APCA also believes that the Commonwealth government, in association with industry, has a role to play in actively encouraging consumers and businesses to move away from using cheques, and towards more efficient methods of payment.

If you wish to discuss any of the matters raised above, or other relevant matters, please feel free to contact myself or APCA's Head of Industry Policy, Dr Brad Pragnell on 02 9216 4888.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Chris Hamilton'. The signature is fluid and cursive, with a long, sweeping underline that extends to the right.

Chris Hamilton  
CEO  
Australian Payments Clearing Association

## **Appendix One: Recommendations to FSI from APCA's August 2014 Submission**

Recommendation 1: APCA believes the current regulatory structure for payments has worked well and substantive revision of payments regulation is unnecessary.

Recommendation 2: APCA recommends promoting competition between schemes over direct regulation. In the context of on-going RBA responsibility for payments policy, APCA further recommends RBA involvement in policy decisions about interchange fee regulation and that the Australian Payments Council could play a role in focussing any industry debate.

Recommendation 3: APCA supports consideration of a “graduated framework” approach for retail payment system regulation. As part of this, APCA would suggest a thorough review of the APRA / RBA purchased payment facility regime as well as the related ASIC non-cash payment facility regime.

Recommendation 4: APCA believes that the new Australian Payments Council has a critical role in advising on how to deal with new entrants and new technologies to minimise the potential for ill-considered intervention by public regulators.

Recommendation 5: APCA recommends that the RBA’s jurisdictional reach under the Payments System (Regulation) Act (PSRA) be reviewed to ensure it can effectively respond to new entrants, increasing technological diversity and increasing marketisation of payment systems and networks.

Recommendation 6: APCA believes that the co-regulatory approach of setting high-level policy objectives, supported by co-ordination and self-regulation by payment system participants to achieve these objectives, is the best way to meet future challenges. The RBA should retain the ability to step in as a last resort if this does not deliver the required outcomes.

Recommendation 7: APCA recommends that inter-regulatory coordination protocols be reviewed in an effort to minimise the burden on regulated entities, particularly smaller organisations, having to deal with multiple regulators.

Recommendation 8: APCA recommends exploring greater economic efficiencies associated with the management of cheque and cash use decline and the promotion of electronic payments including:

- A clear government position on reducing the use of cheques and cash and promoting electronic payments;
- A government policy on coinage to recognise and encourage reduced use of coins;
- Enabling the Royal Australian Mint to accept the return of coins from financial institutions;
- Government support for bridging strategies and education campaigns on the benefits of existing telephone, electronic and online payments aimed at those (typically older Australians, rural and regional communities, and small business) who, today, remain reliant on cheques;

- Preparation of an omnibus bill by the Attorney-General's Department to remove specific references to cheques in Federal legislation. This issue should also be addressed at the Council of Australian Governments (COAG) to ensure parallel take up by state governments; and
- The RBA working with industry to achieve a clear position on charging for cheques and other payment instruments.

Recommendation 9: APCA supports industry and government coordination on cyber-security and sees value in, and would like to be involved with, strategic work on this issue. APCA notes it is important to avoid unnecessary overlap in undertaking any such strategic work.

Recommendation 10: APCA would support the exploration of a national digital identity strategy and suggests that the Australian Payments Council and APCA are well placed to help develop industry-wide views on digital identity that balance security concerns with the need for competition, innovation and efficiency, and the need to promote security and trust for the consumer.