Australian Payments
Clearing Association

17 August 2015

Dr Kathleen Dermody
Committee Secretary
Senate Standing Committees on Economics
PO Box 6100
Parliament House
Canberra ACT 2600
Email: economics.sen@aph.gov.au

Dear Dr Dermody,

Re: Inquiry into matters relating to credit card interest rates

I am pleased to lodge a submission to the Senate Economics References Committee's Inquiry into matters relating to credit card interest rates on behalf of the Australian Payments Clearing Association (APCA). An overview of APCA is provided in Annex I of this letter.

While APCA, as the self-regulatory body for Australia's payments industry, considers matters relating to the payments system, we do not comment on customer pricing as this is a competitive issue for members. I note that the terms of reference for the inquiry included reference to interchange fees, ATM fees and competition in the cards market. These are areas relevant to the efficient operation of the payments system and where APCA has provided its views in the past. We further assert that the Australian payments industry exhibits high levels of competition and innovation.

Interchange Fees and Competition in the Cards Market

The issue of interchange fees is the subject of a review by the Reserve Bank of Australia (RBA) that is currently underway as well as being a matter subject to a recommendation within the Financial System Inquiry Final Report. APCA's views on interchange fees are on the public record and we attach for your information our submission to the RBA Review (see attachment).

APCA's view is that it does not believe there is any clear case for reducing the overall level of interchange fees. Australia has low interchange fees compared to other developed credit card markets, such as those in North America. Further, APCA believes the Australian payments industry is exhibiting high levels of competition and innovation, with the rapid uptake of contactless payments and the introduction of new mobile-based and online payment offerings. Drastic change to the economics of retail payments runs the risk of disrupting existing market dynamics and innovation, with costs ultimately borne by cardholders and merchants.

In respect to the regulation of interchange fees, we remain of the view that the RBA is best placed to act as regulator.

ATM Fees

In respect of ATM fees, the RBA and Treasury undertook a joint investigation into ATM fees in 2011 after the implementation of ATM direct charging reforms introduced in March 2009, and APCA lodged a submission to this review (see attachment). In our submission, we expressed the view that the introduction of direct charging in ATMs appeared to have generated the following benefits:

- dramatic and resilient shifts in consumer behaviour in response to the new price signals;
- consumer savings of an estimated $120 million in ATM fees in the first year of the regime;
- the rise of the independent ATM deployer sector plus new competitive offerings such as fee-rebated accounts and wider fee-free networks; and
- number of ATMs having increased since the reforms.

We argued that many Australian consumers have modified their behaviour in response to direct charging and, in the main, the changes appear to have been positive for the majority of Australian consumers.

We would be more than happy to discuss any aspect of this submission with the Committee. Please feel free to contact myself or APCA's Head of Industry Policy, Dr Brad Pragnell on 02 9216 4888.

Yours sincerely

Chris Hamilton
Chief Executive Officer

Annex 1

About APCA

APCA is the primary industry vehicle for payments industry collaboration in Australia. APCA was established in 1992 to manage and develop regulations, procedures, policies and standards governing payments clearing and settlement within Australia. Historically, its focus has been on the administration of a number of clearing systems, notably the systems for cheques, "direct entry" (bulk electronic payments), aspects of ATM / EFTPOS / card transactions, high value transaction and wholesale cash.

These systems are critical for the secure and efficient operation of the Australian payments system by providing shared self-regulatory rules and procedures for system members. APCA supports these systems through providing secretariat, compliance and other support to member governance groups. In Australia, institutions involved in the payments system have historically exchanged payment messages bilaterally.

As part of its role, APCA maintains device security standards and a number of key industry databases which support the efficient operation of Australian payments, including the BSB database. APCA collects payments statistics that inform member decision-making and provide critical information for stakeholders. This includes information about payment system volumes and values, the number of ATMs and EFTPOS devices in Australia and fraud statistics. APCA provides information to the community about payments through the APCA website, publications and education campaigns. APCA engages with stakeholders bilaterally as well as through APCA-supported initiatives such as the APCA Stakeholder Forum.

APCA has also worked towards a strategic agenda for Australian payments. This has been through the publication of Low Value Payments: An Australian Roadmap (the LVP Roadmap), policy submissions and discussion papers on issues such as the future of cheques, future of cash, online payments and industry co-regulation.

APCA has supported the implementation of new innovation in payments through our industry projects, such as an enhanced communication network the Community of Interest Network (or COIN infrastructure network), and by providing thought leadership and opportunities for discussion about innovation within the industry, in particular through the New Payments Platform and the Australian Payments Council, as well as coordinating the industry implementation of Direct Entry Same Day Settlement.

In recent years, APCA has reformed its governance, opening up membership as well as opportunities to participate in APCA decision-making. This has resulted in APCA appointing three voting independent directors. As well our membership has been opened beyond clearing system members to a wider range of payment organisations.

More information about APCA can be found at www.apca.com.au

APCA Submission to the RBA Review of Card Payments Regulation

April 2015

About this document

This document has been prepared by the Australian Payments Clearing Association Limited (APCA).

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Note

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

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Executive Summary

The Australian Payments Clearing Association (APCA), as the industry association and self-regulatory body for Australian payments, is pleased to make this submission to the Reserve Bank of Australia's Review of Card Payments Regulation Issues Paper ("Issues Paper").

For many years, APCA has been an active participant in debates on the regulation of card payments, and welcomes this further opportunity to make a contribution to an important element of payments policy in Australia. Throughout this debate, our preference has been to maximise the opportunity for competition and transparency to drive good outcomes such as efficiency and choice, so that any regulatory intervention should be targeted to complement market-driven outcomes rather than to replace or compensate for them. This remains our objective.

The Issues Paper firmly positions the current review as a further evolution on past reforms (page 25). As such, the focus is on modifying the current regime of interchange fee regulation to address particular concerns, rather than revisiting the underlying rationale in any holistic way. Critical to this premise is the explicit assumption that the market will continue to be largely composed of mature major card schemes that are viewed as a "must take" method of payment for merchants (see page 8). We believe that this characterisation significantly understates the degree of change in the competitive dynamics of the marketplace, and that the rate of change, innovation and competition is in fact increasing.

This has two major implications. First, the substantial changes in competitive dynamics since the implementation of regulation will warrant a thorough review of the underlying basis for regulation within the next three to five years. In light of significant technology change, it is highly likely that the competitive dynamics of retail payments will, by then, be markedly different.

Second, any changes made now to address specific concerns may have a short life expectancy. Industry-wide change driven by an extensive new compliance regime is unlikely to meet any reasonable industry cost/benefit test, if, as we submit, the market dynamics are evolving rapidly. There is a risk that industry and regulatory effort and cost is expended on incremental change that needs frequent revision as market dynamics change. This does not deny the potential value of targeted changes to address specific concerns.

We do not believe there is any clear case for reducing the overall level of interchange fees. Australia already has amongst the lowest rates in the world. On the contrary, whatever level interchange fees restrictions are set at, the market will adjust around the new regulatory impost with the supposed benefits for consumers remaining unmeasurable. We also believe the Australian industry is exhibiting high levels of competition and innovation. Drastic change to the economics of retail payments runs the risk of unintended consequences in terms of existing market dynamics.

That said, we do believe some of the matters raised in the Issues Paper would benefit from attention in the short term, provided this does not impose industry-wide structural change. An important component of effective competition is transparency. We recognise that the number and range of interchange fee rates creates a lack of transparency for merchants of the costs they will incur. The effect of the upper rates also creates a perceived unfairness of outcomes between small and large merchants.

Therefore changes to the frequency of the weighted average calculation and an upper cap on the highest single interchange fee rate may be warranted to enable better management of costs for individual merchants. We do not support a mandated technological or regulatory solution to provide merchants with “real-time” information on the costs of an individual transaction as it would be unlikely to meet the cost/benefit test. We would however support further exploration of disclosure-based measures to improve the transparency of costs to merchants.

Regulatory support for surcharging, though intended to provide an avenue for recouping merchant costs and conveying price signals, has in practice opened an avenue for the exercise of merchant power in particular markets. This is not fundamentally a payment system issue, but a competition issue in those markets. APCA does not support the recommendation in the Financial System Inquiry Final Report to create a system-wide three-tiered approach, since it represents an expensive system-wide compliance solution for specific problems in particular markets. Consumers experience excessive surcharging in particular industries and as such the solution to excessive surcharging should be to target those industries where this practice is most common.

Further, APCA believes that American Express currently operates as an easily distinguished competitor, and one that is in no way a “must take” for any merchant. Given our concern to avoid large-scale and costly structural change for relatively narrow benefit, we see no regulatory rationale for and would not recommend that the regulatory perimeter be extended to include financial institution-issued American Express cards.

APCA believes that cardholders should be able to decide which account and scheme should be used for a transaction. Enabling merchants to decide on routing will only benefit larger merchants (who would have the capability to introduce the technological changes and the market power needed to benefit from this) and, as such, exacerbate the gap between the costs experienced by large and small merchants.

Lastly, APCA would recommend that at the conclusion of this review the Payments System Board focuses on high-level objectives and, if required, that industry assist in working towards efficient and workable solutions and implementation paths.

Recommendations

Recommendation 1: APCA recommends that the next review of retail payments regulation should occur within the next three to five years, should holistically review developments both within and beyond card payments, and focus on regulatory approaches that harness and improve the competitive marketplace. In particular, the ongoing utility of interchange fee regulation should be reviewed.

Recommendation 2: APCA recommends that changes to interchange fee regulation arising from specific concerns raised in the current Review should be subjected to careful cost-benefit implementation analysis, so as to ensure that transitional and compliance costs do not outweigh perceived benefits.

Recommendation 3: APCA recommends that competitive and disclosure-based solutions to enhanced merchant information be sought rather than a regulatory and mandatory technical solution.

Recommendation 4: APCA recommends retaining the weighted average with annual recalculation.

Recommendation 5: APCA recommends an exploration of a cap on the highest individual interchange fee rate that a regulated scheme could offer, as well as a possible limit on the number of different interchange fee rates.

Recommendation 6: APCA recommends that the FSI recommendation for three-tiered surcharging not be pursued but rather targeted measures be explored.

Recommendation 7: APCA recommends that clarity be provided on the ability to surcharge non-card payments instruments.

Recommendation 8: APCA does not support further extending interchange fee regulation to additional schemes.

Recommendation 9: In responding to the Review, the Payments System Board should focus on articulating high-level policy objectives and seek engagement with industry on identifying solutions and implementation paths.

1. Overall Views on Card System Regulation

1.1. Interchange Fee Regulation

Interchange fees are a form of wholesale pricing and their regulation represents a significant intervention into the operation of the market. Prices should ideally be set by the market and APCA believes promoting competition is generally preferred to price regulation.

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 jurisdictions. There is nothing approaching a clear consensus on the optimal regulatory approach. As always in matters of competition policy, APCA submits that the need for regulation remains contingent on the evidence, and in particular on whether there is effective competition in each of the markets in the value chain.

The Issues Paper suggests that increased scheme competition might perversely have the effect of driving upward interchange fees and other costs for acquirers and merchants (page 4). This assertion is only true where competitive pressures on the acquiring side of the two-sided market represented by the payment network are less than on the issuing side. Critical to this premise is the explicit assumption that the market will continue to be largely composed of mature major card schemes that are viewed as a "must take" method of payment for merchants (see page 8).

Contrary to this assumption, there is strong evidence that increased competitive pressure through more intense scheme competition and greater commercial freedom for merchants through relaxed honour-all-cards restrictions, and the ability to surcharge, have increased the market power of large merchants to the point where they can negotiate lower interchange fees than the cap – the strategic merchant rates discussed on pages 26-28 of the Issues Paper. The Issues Paper does not recognise this outcome as being driven by greater competitive pressure on schemes, but it does identify the consequential issue that merchants with less market power bear relatively higher rates.

This evidence highlights that competitive pressures are working in card payments and potentially can be made to work better.

1.2. Changes in the Market

In previous reviews such as the one undertaken in 2007/08, the Payments System Board (PSB) linked competition with interchange fee regulation. If the competitive dynamics were appropriate and certain innovations (such as new online payments) were introduced, then the PSB indicated it would consider stepping back from interchange fee regulation. More recently, the Financial System Inquiry (FSI) Final Report recommended that the PSB consider extending and strengthening interchange fee regulation.

Conversely, APCA has, in forums such as the FSI, questioned the long term sustainability of such regulation. APCA's concern is that the FSI report seems to regard low interchange fees as an inherent good, whereas the original regulatory rationale was to address a perceived market failure whereby merchants were unable to exert market power in relation to schemes. The RBA has acknowledged that interchange fees may have a legitimate role to play in balancing incentives within a two-sided market and to help it grow. This could apply in the establishment of a new system (such as an NPP overlay service). We submit that this policy approach is preferred.

The competition dynamics facing payment schemes and systems have fundamentally changed since interchange fee regulation was first introduced. MasterCard and Visa have become independent commercial organisations in 2006 and 2008 respectively; in 2009 eftpos Payments Australia Ltd was established as a separate commercial organisation enabling it to compete with the card schemes and in 2014, NPP Australia Ltd was established to implement a faster payments infrastructure that is likely to facilitate non-card mobile payments. Cards are increasingly used in the online world where there are a number of competing alternatives such as PayPal and other new entrants have entered this market, such as POLi and Paymate. Further, digital currencies offer even newer ways of paying online.

Technology is likely to further change competitive dynamics in the next few years. As physical cards give way to mobile apps and wallets, with new offerings such as Apple Pay, schemes are likely to come under increasing competitive pressure, so that regulation of scheme interchange fees will be affecting a narrowing segment of the total value chain that determines cost to end user merchants and consumers. The regulatory framework must remain robust and responsive to the needs of providers and end users within this changing environment.

1.3. Examining Competition and Long-term Sustainability of Regulation

In APCA's submission to the FSI, we stated that there has been little consideration of the long-term sustainability of regulatory intervention in interchange fees, particularly as technology and competition in payment services evolve. Further, we stated that we believed that 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.

We believe an understanding of this intensifying competition will help inform an appropriate long-term policy response. Though the current Issues Paper appears to be focussed on immediate issues, we believe that the changes in the market since the implementation of regulation, together with technology-driven changes likely in the next few years, warrant a thorough review of the regulatory rationale. Given the accelerating pace of change, the next, more fundamental, review should be within the next three to five years, rather than the five to seven year periods we have seen between previous interchange fee regulation reviews.

Recommendation 1: APCA recommends that the next review of retail payments regulation should occur within the next three to five years, should holistically review developments both within and beyond card payments, and focus on regulatory approaches that harness and improve the competitive marketplace. In particular, the ongoing utility of interchange fee regulation should be reviewed.

1.4. Cost/Benefit Implications of a Dynamic Marketplace

The observations made above relating to changes in competitive dynamics in the last few years, and the likelihood of further technology-driven changes in the future, also suggest a cautious and targeted approach to addressing any specific regulatory concerns in the short term. Making any significant change to the overall structure of interchange fee regulation will impose significant transitional costs on issuers, acquirers and schemes. These costs will ultimately be borne by cardholders and merchants. To unwind existing commercial arrangements would also be complex, costly and difficult.

In a changing environment, regulatory changes with high transitional costs, and changes that create industry-wide compliance costs, are unlikely to be of net value if they require further change within a few years, even if there are material policy benefits. Such an environment also creates a high risk of further unintended consequences, and the need for yet more regulatory adjustment.

Recommendation 2: APCA recommends that changes to interchange fee regulation arising from specific concerns raised in the current Review should be subjected to careful cost-benefit implementation analysis, so as to ensure that transitional and compliance costs do not outweigh perceived benefits.

2. Interchange Fee Developments

Notwithstanding our previously stated position on the long-term sustainability of interchange fee regulation, below APCA offers its views on how the identified issues confronting small merchants may be addressed through modifications to the existing regime, with a focus on enhancing competition and transparency.

2.1. Addressing Transparency for Merchants

The Issues Paper notes that the number of interchange fees rates has increased, leading to complexity. The widening of the range and lower rates for "strategic merchants" can be seen as evidence of increased market power for large merchants relative to schemes. However, it has also meant that smaller merchants, particularly those that have agreed to "interchange fee plus" pricing, are often subject to higher per transaction costs, especially if their customers use premium cards. The Issues Paper also notes that the move towards "account-based processing" similarly obscures the link between the card being accepted and the associated cost to the merchant.

While we would assume the developments noted above have caused some level of dissatisfaction amongst small merchants, further clarity on the scale and nature of the problem would assist in determining an appropriate response. Further, in making any changes, the public policy objectives should be clear. If the underlying public policy objective is one of achieving fairness between small and large merchants, then this should be clearly spelt out.

The Issues Paper suggests that there may be means, both visually and electronically, to make the interchange fee associated with a particular card identifiable to the merchant at the point of acceptance. The costs and benefits associated with enhanced transparency need to be carefully considered. For example, merchants knowing the cost of accepting a card at the time of the transaction may be desirable. However, it is difficult to imagine a situation where a significant number of merchants will make discrete decisions for each type of card based on "colour", given that most merchants are seeking to provide a good customer experience and will rely on simple acceptance and surcharging rules.

As it is difficult to imagine discrete merchant decision-making on each transaction, we would not endorse any regulatory requirement for a "real-time" technological solution, particularly given the lack of clarity on the scale and nature of the problem. Rather we would support acquirers being able to compete and innovate.

We believe that the marketplace for merchant acquiring is competitive. Given the contractual relationship between the merchant and the merchant acquirer, it is probably more important for the merchant to understand the arrangement they are entering into than to receive "real-time" information. On this basis, we would support an exploration on enhancing transparency for merchants through improvements to the up-front and ongoing information they receive from acquirers.

Recommendation 3: APCA recommends that competitive and disclosure-based solutions to enhanced merchant information be sought rather than a regulatory and mandatory technical solution.

2.2. Addressing Interchange Fee Rates

The widening range of interchange fee rates and the upward drift in the highest rate are outlined as matters for concern in the Issues Paper, particularly their impact on smaller merchants, which is identified but not quantified. While these developments could be perceived as going beyond the "intent" of the earlier reforms, they can also be seen as a reasonable and competitive response by Visa and MasterCard to the issuance of American Express cards.

The Issues Paper identifies the transparency of costs for small merchants as an important issue, though as noted above the costs and benefits of intervention remain unclear. On this basis, we would recommend that the PSB focus its response on ensuring the future management of current trends.

2.2.1. Weighted Average versus Hard Cap

The Issues Paper raises concerns about the weighted average and explores the use of a "hard cap". The weighted average provides flexibility in interchange rates and ensures some level of competitiveness between schemes. A hard cap could see the maximum become the minimum and certain groups, such as charities, could lose their zero interchange status. A more frequent calculation of the weighted average may help manage outcomes, though the benefit of this should be weighed up against the cost of more frequent calculation.

Recommendation 4: APCA recommends retaining the weighted average with annual recalculation.

2.2.2. Cap on Highest Individual Interchange Rate

As noted above, the impact on small merchants of the widening range of interchange fee rates and the upward drift in the highest rate appears to be one of the major concerns outlined in the Issues Paper. Graph 9 of the Issues Paper illustrates the trend (see page 21).

If the PSB is concerned about the trend identified in Graph 9 becoming more pronounced, for example the highest rate rising to 250 or 300 basis points, then consideration could be given to a cap on the highest rate. This could be done in a way that does not overly disrupt existing arrangements, prevents a continuation of the existing trends and still provides an opportunity for competition.

Given the concerns about the number of rates (as noted in Table 1 on page 27 of the Issues Paper), consideration could be given to an upper limit on the number of rates. This similarly places a brake on current trends and should dampen increasing complexity but also limits competition and innovation. Any upper limit on the number of rates cannot be “set and forget” but must be flexible to accommodate innovation.

Recommendation 5: APCA recommends an exploration of a cap on the highest individual interchange fee rate that a regulated scheme could offer, as well as a possible limit on the number of interchange fee rates.

2.3. Overall Level of Interchange Fees

The Issues Paper highlights certain overseas initiatives, such as the European Union moving to 30 and 20 basis point caps on credit and debit cards respectively, as a basis for moving to a hard cap and reconsidering the overall level of interchange fee regulation. Using the EU as an example is not without its challenges. As noted in the Issues Paper, these regulations have yet to be approved by the European Parliament and the Council of the EU. Under the current proposal, member countries have flexibility in how they would be implemented.

Further, the payments market in most EU countries is quite different than that seen in Australia (or jurisdictions such as Canada or the UK). As noted in the Issues Paper, overall credit card use throughout continental Europe is modest.

A jurisdiction which has a profile more akin to Australia is Canada where in late 2014, Visa and MasterCard agreed to a five year commitment effective April 2015 to reduce their effective (average) interchange fee rates to 150 basis points. There was also commitment on new lower rates for charities and independent businesses such as newsagents and pharmacies. This voluntary commitment has been incorporated into the Canadian Code of Conduct changes announced by the Canadian Minister of Finance on 13 April 2015. [1]

On this basis, it is hard to see Australia being “out of step” with overseas developments by retaining the 50 basis point weighted average.

Further, in the 2007/08 Review, in considering a move from 50 to 30 basis points, the RBA sought industry commitment to enhanced innovation through the development of eftpos Payments Australia Limited (ePAL) and a new online payments offering. The Australian industry, has in recent years, demonstrated its commitment to enhancing competition and innovation through the development of ePAL and commitment to the New Payments Platform.

[1] http://news.gc.ca/web/article-en.do?nid=962329, Accessed 19 April 2015.

3. Surcharging

3.1. Excessive Surcharging

"Excessive surcharging" occurs when surcharges are perceived to be higher than the costs of card acceptance. Excessive surcharging is a concern, as it distorts price signals and adversely impacts on payments system efficiency.

APCA acknowledges that excessive customer surcharging remains a controversial practice that requires close attention. Ideally the surcharge should reflect the cost of acceptance. However in practice, 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. This includes the application of existing consumer protection provisions on pricing.

As excessive surcharging is often concentrated in particular industries, the solution may also be targeted. The approach of the Victorian Government to regulating surcharging within the Victorian taxi industry represents one way in which a targeted approach could address community concerns.

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.

Recommendation 6: APCA recommends that the FSI recommendation for three-tiered surcharging not be pursued but rather targeted measures be explored.

Given the RBA's objective for payments efficiency, there should be clarity on the ability of merchants to surcharge both card and non-card payment instruments to recoup acceptance costs and to effect more robust payment instrument competition.

Recommendation 7: APCA recommends that clarity be provided on the ability to surcharge non-card payments instruments.

4. Other Issues

4.1. Competitive Neutrality

APCA supports competition and transparency. In respect to American Express, including financial institution-issued cards, competition and price signals appear to be operating. Merchants have been able to distinguish American Express from other cards and have often chosen to refuse or surcharge these cards.

It is our belief that the issue of competitive neutrality and companion cards is an outcome of the limitations of the current approach which relies on designation of individual payment systems. This approach works well in an environment where the number of different payment methods and schemes are stable and well-defined. New entrants, new technology and deepening competition in the scheme space expose some of the difficulties of this approach. Imposing similar requirements on designated schemes is a difficult and time-consuming process, particularly where different business models and fees structures are used. As well, non-designated schemes may retain a competitive advantage.

Despite these anomalies and recognising the challenge this creates for the regulated schemes, interchange fee regulation being extended to another scheme does not address the long-term unsustainability of this regulatory approach.

Recommendation 8: APCA does not support further extending interchange fee regulation to additional schemes.

Publishing thresholds as to when an entity will be subject to interchange or related regulation would assist in providing transparency and enabling entrants to make decisions about entering the Australian market. This approach will require the development of objective criteria and the collection of accurate data, both of which will prove challenging. If possible, this could be an improvement on the current situation. However, it also points to the underlying problems with the current approach and that interchange fee regulation is not a sustainable long-term solution.

4.2. Routing

The RBA is seeking views on clarifying arrangements for competing payment options within a single device or application.

The introduction of contactless cards has made this an urgent issue and the development of new types of digital wallets and the use of mobile technology will only exacerbate the challenge of who sets the default, who can override that and on what basis they can do so. Clarity on this is important as is working towards an outcome that supports robust scheme competition and provides transparency for both cardholders and merchants.

APCA believes that the following principles should be applied:

- That the cardholder should be able to choose which account or scheme is used when making a transaction where choice is available and not have that choice changed without their knowledge and consent;
- That no one scheme should be able to unfairly restrict or inhibit the ability of another to compete;
- Maximising interoperability of cards instruments, terminals and host processing is desirable;
- Respecting the confidentiality of commercially sensitive data;
- Maximising the operational efficiency of the system; and
- Promoting innovation in card services and products.

The “dual-network debit card” announcement by the RBA on the 21 August 2013 provides a high-level indication as to the agreement the RBA reached with the card schemes. However details of this agreement are not in the public domain and, as a result, it is difficult for APCA to comment.

Further, enabling merchant routing may have the unintended consequence of benefitting larger, established players that are able to make the investment to take advantage of routing while smaller players may be unable to do so.

5. Process

As the PSB develops its response to this Review, APCA would recommend that the PSB work towards high-level policy objectives and then for industry to work towards an agreement on a specific solution / implementation. This approach was successfully employed in the Strategic Review of Innovation, by providing both public policy direction but also relying on industry expertise to explore and craft a more efficient and workable outcome.

APCA and the Australian Payments Council could play a role in developing an industry response, with APCA potentially playing an important role in implementing policy. Further assistance could be provided through APCA's Issuers and Acquirers Community and engagement with the main schemes, which are now Operator Members of APCA. This could be done in an open and inclusive fashion.

Recommendation 9: In responding to the Review, the Payments System Board should focus on articulating high-level policy objectives and seek engagement with industry on identifying solutions and implementation paths.

6. Conclusion

APCA continues to believe that competition and transparency should be promoted rather than regulation imposed. We also believe that interchange fee regulation is unsustainable in the face of technological and commercial developments.

Any changes to the existing regime should be subject to careful scrutiny to minimise any transitional costs. However, APCA believes that there may be changes to the existing regime, such as changing when the weighted average is calculated and an upper limit on the highest interchange fee rate, which could be done in an efficient fashion and which address the concerns of small merchants over the number, complexity and range of interchange fee rates.

The Australian industry has demonstrated, through initiatives such as the New Payments Platform, its ability to find solutions to seemingly intractable and complex industry issues. On that basis, the PSB should seek to establish high level policy objectives with the industry engaging collaboratively to find meaningful and workable solutions and implementations.

Australian Payments
Clearing Association

SUBMISSION TO THE RBA-TREASURY ATM TASKFORCE

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Australian Payments Clearing Association

About this document

This is a submission of the Australian Payments Clearing Association to the RBA-Treasury ATM Taskforce inquiry into the implementation of ATM reforms introduced in March 2009.

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1. The Inquiry

The Australian Payments Clearing Association Limited (APCA) welcomes the opportunity to make this submission to the RBA-Treasury ATM Taskforce ("the Taskforce").

The Taskforce will report to the Treasurer by June 2011 on the implementation of ATM direct charging reforms introduced in March 2009. The report will consider the impact of the reforms on:

- The transparency and level of ATM fees;
- Consumer behaviour;
- Competition in the ATM market; and
- The deployment of ATMs.

The Taskforce has requested APCA provide its initial views on these issues by Friday, 15 April 2011. APCA looks forward to further discussions with the Taskforce as its work progresses.

2. APCA's Role

APCA was the coordinator of the industry's implementation of ATM direct charging and undertook a public education campaign in the lead up to direct charging. APCA worked with a wide range of key industry stakeholders to provide coordination of the significant industry efforts involved in the implementation of direct charging.

APCA also has also a key role in Australia's ATM system through management of the Consumer Electronic Clearing System (CECS).

3. The transparency and level of ATM fees

The ATM direct charging reforms were designed to ensure transparency in ATM charges. Removal of the interchange fees paid between ATM issuers and acquirers and the move to direct charging would enable users of ATMs to know how much they were actually paying to use a "foreign" ATM. Similarly, the decision by most financial institutions in Australia to not charge their account-holders a "foreign fee" has further enhanced the "real-time transparency" of ATM-related charges paid by consumers.

Though there has been some commentary that the $2.00 direct charge dominates, there is a reasonable amount of variability for direct charging. A number of independent deployers have chosen to charge higher amounts for withdrawals, for example $2.20 or $2.50. Alternatively, some financial institutions have chosen to charge less, including one major financial institution which charges $1.50 for withdrawals and 50 cents for balance inquiries. Recently released RBA research notes that three-quarters of ATM transactions are not

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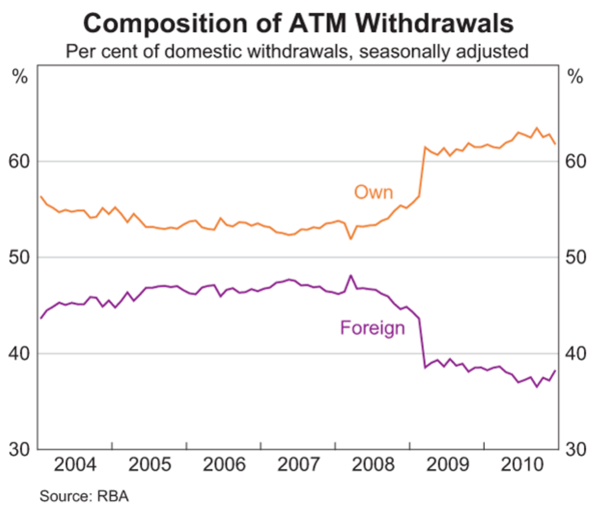
subject to the direct charge.[1] Further, concerns expressed over the specific level of fees charged by individual ATM providers must be put in the context of consumer savings of an estimated $120 million in ATM fees in the first year of the regime.[2]

4. Consumer behaviour

A significant reason for these savings has been a result of customers changing their behaviour, in response to more transparent pricing. When the ATM reforms came into place in March 2009, there was an immediate and dramatic shift in customer behaviour away from "foreign" and towards "own" ATM withdrawals (see below). Similarly there was an increase in EFTPOS cash-outs.[3] Over 60 per cent of ATM withdrawals continue to be from "own ATMs", demonstrating consumer behaviours have remained resilient.



The observed change in consumer behaviour suggests that Australian consumers are keenly aware of direct charging and able to modify their behaviour accordingly. These developments should read alongside recent research that suggest consumers who paid direct charging do so knowingly for convenience reasons.[4] These findings suggest that arguments that consumers are somehow under-informed about direct charging appear ill-founded. Further, policy responses to address any such "information gap", such as additional on-screen notifications and/or additional external signage, would therefore appear to be questionable benefit.[5]

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[1] Flood, D., Hancock, J. and Smith, K (2011) "The ATM Reforms – New Evidence from Survey and Market Data", *RBA Bulletin March 2011,* p.44

[2] Ibid, p. 43.

[3] Ibid, p.44 Also APCA (2010) 'ATM direct charging – Trends one year on " *Payments Monitor*, First Quarter 2010, available at http://www.apca.com.au/PM/2010 Quarter1/5.html

[4] Flood et al (20110, p.46.

[5] Fear, J (2011) *The price of disloyalty: why competition has failed to lower ATM fees.* The Australia Insitute and CHOICE, Policy Brief No. 23, February 2011. p.4.

5. Competition in the ATM market

The Australian ATM market appears to be highly competitive. About half of the machines in Australia are operated by organisations that are independent of the major financial institutions. The two largest ATM deployers in Australia (Customers ATM and Cashcard) are independent and each have about 20% of machines in Australia. Between them, the four major financial institutions have about 40% of the ATMs deployed in Australia. This stands in sharp contrast to the situation found when the RBA / ACCC 2000 Joint Study was undertaken and the four major financial institutions had approximately 65% of ATMs.[6]

Direct charging lowers barriers to entry by providing independent deployers with a revenue stream direct from cardholders rather than one reliant on negotiating interchange fee arrangements. Indeed, the largest deployer of ATMs in Australia, Customers ATM, entered the ATM market in 2003. [7]

Direct charging has also opened up new forms of competition, including the rise of fee-free networks and a number of financial institutions providing offerings where they rebate much of the cost of the direct charge to their account-holders.[8] The emergence of fee-free networks has been notable with "the largest 30 financial institutions in terms of ATM usage, 28 institutions (covering 98 per cent of all ATM cardholders) … providing access to a network of at least 1500 ATMs charge free or at reduced charges to their cardholders"[9].

6. The deployment of ATMs

Past overseas experience strongly suggests that the introduction of a direct charging regime results in a rise in ATM numbers. [10] Australia appears to have followed this trend. The number of ATMs in Australia has risen from 25,658 in June 2008 prior to the introduction of the reforms to 28,764 by June 2010. [11]

Recent RBA research also indicates that the dispersion of ATM growth has been evenly distributed between metropolitan, non-metropolitan and remote regions, allaying concerns that growth would be concentrated in already well-serviced metropolitan locales.[12]

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[6] RBA/ACCC (2000) *Debit and Credit Card Schemes in Australia: A Study of Interchange Fees and Access*, October 2000, p. 13.

[7] http://www.customersatm.com.au/about-us/history/ . Accessed 14 April 2011.

[8] Filipovski, B. and Flood, D. (2010) "Reform of the ATM System – One Year on", *RBA Bulletin June 2010*, p. 37.

[9] Ibid., p.42

[10] McAndrews, J. (2003) "Automated Teller Machine Network Pricing – A Review of the Literature", *Review of Network Economics*, Vol 2. No. 2, pp. 146-158.

[11] APCA statistics. Available at www.apca.com.au.

[12] Flood et al (2011), p. 48.

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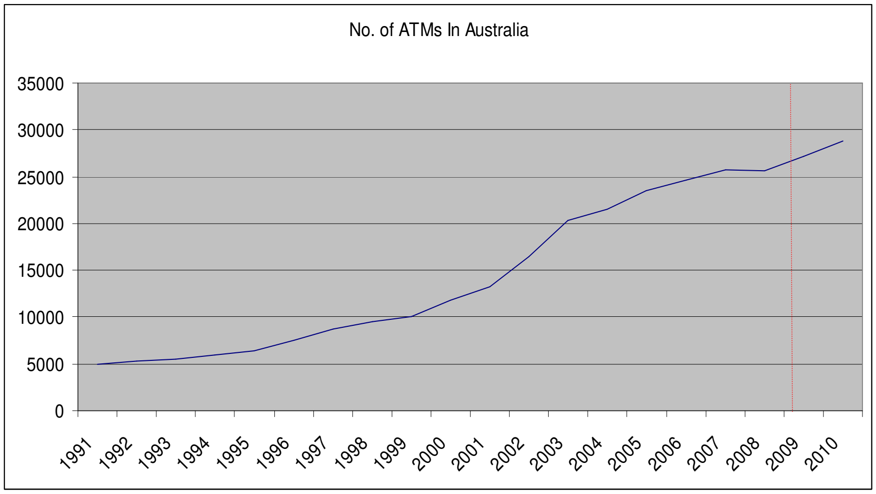

Source: APCA

7. Conclusion

The implementation of ATM direct charging was a significant undertaking for the industry. APCA, in its role as coordinator of the industry's implementation, keenly recognises the challenges involved in undertaking these type of systemic changes.

The objectives of the ATM reforms were to improve price transparency, promote competition and increase ATMs deployed in a wider variety of locations. Over the past two years, the reforms appear to have broadly achieved these objectives. Evidence of this includes:

- dramatic and resilient shifts in consumer behaviour in response to the new price signals;
- consumer savings of an estimated $120 million in ATM fees in the first year of the regime;
- the rise of the independent ATM deployer sector plus new competitive offerings such as fee-rebated accounts and wider fee-free networks; and
- ATMs having increased from 25,658 to 28,764, or 12.1%, since the reforms.

Many Australian consumers have modified their behaviour in response to the new regime and, in the main, the changes appear to have been positive for the majority of Australian consumers.