

15 October 2004

Dr John Veale
Head of Payment Policy
Reserve Bank of Australia
65 Martin Place
Sydney NSW 2000

Dear Dr Veale,

EFTPOS Interchange Fees

This submission is in response to the RBA press release of 9 September 2004 relating to the desirability of setting standards for interchange fees for the EFTPOS debit card and Visa Debit payment systems.

MoneySwitch Ltd made a submission to the RBA on 7 July 2004 relating to the possible designation of EFTPOS System as a payment system and the comments there provide some additional background to this submission. As a brief summary, MoneySwitch Ltd is in the process of becoming an acquirer of credit cards, following the RBA release in early 2004 of an access regime relating to credit card acquiring. It is a marketplace imperative that MoneySwitch must also offer EFTPOS debit card and Visa Debit acquiring services.

Interchange Fee and Access Regime Interrelated

A new acquirer must establish a debit interchange agreement with each of the seven current Tier 1 EFTPOS financial institutions, either directly or via a higher cost gateway provider. This agreement must cover interchange fees as well as technical and contractual arrangements relating to the establishment, testing and ongoing maintenance of the interconnection links.

MoneySwitch is strongly of the belief that interchange fees cannot be determined in isolation without also having a complementary, industry wide access regime. The access regime must impose determinable conditions relating to setup costs, timescales and sharing of ongoing communications, maintenance and support costs. If the interchange fee is determined without defined industry access conditions, then the lack of access conditions will exclude new entrants, and the desired competition and efficiency will not be achieved

Interchange Fee must be Objectively Determinable

Because of the bilateral nature of this interchange fee, there is currently no way for this to be objectively determined in discussions between a new acquirer and an existing issuer. An acquirer must deliver transactions to each issuer. There is no market where competing fees for that issuer's transactions can be provided, because the transactions can go only to that one issuer. In the absence of an externally determinable interchange fee, the different market strength of the incumbent issuer and a new acquirer means that the new acquirer must take any price offered.

In order to allow new entrants on a level playing field, it is essential that the interchange fee can be objectively determinable by each party, and that the interchange fees are the same for all participants.

Level of Interchange Fee

An acquirer has very similar costs for the provision of acquiring services for debit cards and for electronic authorisation of credit cards. It uses the same merchant terminal, the same acquiring network, and has similar costs for switching to the issuers. It requires similar settlement arrangements, and similar sales and support costs.

Credit card acquiring has some increased costs because of slower issuer settlement and for fraud and chargeback costs, while debit card acquiring has higher costs in the area of security processing. These differences in costs are small compared with the overall costs of processing transactions.

Given that credit card acquiring is an attractive business even with significant positive interchange fees, MoneySwitch does not believe that a negative interchange fee is necessary to provide a competitive debit card acquiring offering.

The costs of acquiring are passed to the merchants, typically as a monthly terminal fee and a processing fee, either per transaction or ad valorem. MoneySwitch believes that any interchange fee will be effectively passed on to the merchants; whether these interchange fees are zero, positive or negative.

MoneySwitch believes that a zero interchange fee will lower the cost to cardholders using debit cards and will make the use of debit cards relatively more attractive compared with credit cards. This will increase use of debit cards, which have a lower cost to the merchant than accepting credit cards with their positive interchange fee.

Interaction with Access Conditions

The total fees seen by merchants will be lower if there is effective competition in the acquiring marketplace. Competition in the acquiring marketplace will drive down pricing, producing benefits for the merchants and the economy as a whole.

Setting a zero interchange fee in of itself will not facilitate competition unless there is certainty of access on reasonable terms and in a reasonable timeframe, and that any fees associated with access do not have the effect of circumventing the multilaterally-set interchange fee. There must also be no method of exclusion from access of new entrants because they have a low volume of transactions.

The costs of access can be broken into initial costs and ongoing costs:

1. Initial Costs.

These costs cover establishment, project management and testing of the communications links and settlement procedures between a new entrant acquirer and each existing issuer. We accept that the access seeker should pay reasonable and determinable costs for the new attachment.

The costs should be based on the average cost of providing connections, and the new entrant should not have to pay to full cost of any new equipment that has the possibility of providing additional facilities or processing for other connections.

The establishment cost should be determinable by a formula, and should be reasonably consistent from one access provider to the next.

2. Ongoing Costs.

It is essential that ongoing equipment, communications and support costs are shared by the access seeker and the access provider. Each party must pay its own costs. There must not be payments from one side to the other, since these would have the effect of being an additional interchange fee.

Because each party carries its own costs, this will send price signals to each party. It will cause the most cost effective facilities to be used and will cause these facilities to be cost-reduced over time as new technologies become available.

Summary

MoneySwitch believes that a debit card interchange fee should be set by the Payment Systems Board on a multilateral basis. We further believe that an interchange fee that is set to zero will encourage the use of debit payment instruments by cardholders and will lower the total cost of payment processing to the economy.

However, it is essential that there is a set of access rules in place at the same time to ensure that new entrants can gain access with reasonable and determinable costs, times and conditions. It is further essential that each party must cover its own ongoing costs of communications and support, so that this does not become a de facto additional interchange fee.

Sincerely,

A handwritten signature in black ink that reads "Paul A Wood".

Paul A Wood
CEO, MoneySwitch Ltd
<http://www.moneyswitch.net>