



AUSTRALIAN BANKERS' ASSOCIATION INC.

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Mr Glenn Stevens
Governor
Reserve Bank of Australia
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Dear Governor 

Proposed changes to the EFTPOS interchange fee standard

The Australian Bankers' Association (ABA) Council has argued for some time for the deregulation of interchange fees in Australia, in terms of credit cards, EFTPOS and scheme debit systems.

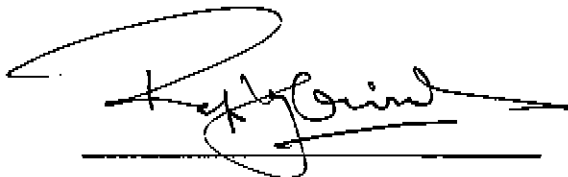
We acknowledge that the Reserve Bank has indicated a preference for this direction as well, and we understand its stated pre-condition for such an outcome – that of sufficient competition on interchange fees.

With the Reserve Bank's recent move to defer the decision on the future of interchange regulation, achievement of the ultimate deregulatory objective is still uncertain. This is of some disappointment to the industry, although we are confident that in time the objective can be successfully achieved.

We thus welcome the Reserve Bank's current consultation with respect to proposed changes to the EFTPOS Interchange Fee Standard announced 22 September 2009.

We are supportive of the proposed changes to EFTPOS regulation. A movement to regulatory parity with scheme debit is essential for the long term health of EFTPOS. I attach a Submission detailing the reasons for this support. The ABA Executive Management is available to discuss this Submission at any time.

Yours sincerely,



Ralph Norris

CC:
Michele Bullock, Head of Payments Policy, Reserve Bank of Australia.
David Bell, CEO, Australian Bankers' Association.

ABA Submission

Background

The Australian Bankers' Association (ABA) has advocated for some time the deregulation of interchange fees in Australia, in terms of credit cards, EFTPOS and scheme debit systems. We acknowledge the Reserve Bank's indication that this is its preferred approach as well.

The ABA has supported reforms over the years aimed at improving the competitive environment, such as new access regimes and the removal of merchant pricing restrictions, but the ABA has maintained its opposition to interchange regulation on the grounds that interchange regulation is inconsistent with the competition objective.

More recently, in terms of promoting competition, the ABA Council has supported the establishment of a commercial scheme to better operate the EFTPOS network (EFTPOS Payments Australia Limited) and BPay's Project MAMBO – a step-change initiative to improve customer choice and promote competition.

The RBA's recent deferral to its final decision on the future course of interchange fees leaves the competition and regulation issue unresolved. We understand that one consequence of this is that it is now necessary to deal with the regulatory anomaly between EFTPOS and scheme debit. Ultimately, however, we see the optimal pro-competitive approach as full deregulation of interchange fees.

ABA view on the proposed change to the standard

The ABA supports the Reserve Bank's recommendation that EFTPOS interchange fee regulation be put onto the same footing as that applying to Visa Debit and MasterCard debit.

Currently, EFTPOS interchange fees are capped at between 4 and 5 cents on an average transaction, with the fee paid from card issuer to merchant acquirer. This contrasts with the regulatory rules applying to MasterCard Debit and Visa Debit which allows a weighted average interchange fee of 12 cents payable to the card issuer.

The problem with this differential is that it restricts the freedom of EFTPOS Payments Australia and its participants to compete on the grounds of comparable and consistent economic arrangements.

Adopting a consistent regulatory framework will be more conducive to future investment and would help incentivise participants to provide the support and promotion of EFTPOS that is essential to its future. Redressing current regulatory arrangements that place restrictions on EFTPOS participants that do not apply in regard to Visa Debit and MasterCard debit is vital.

Competition implication

By having different regulatory approaches to scheme debit cards as that of EFTPOS, the regulations imbed a distortion with potential competitive implications. If, for example, it is more optimal for EFTPOS interchange fees to be 12 cents (and flow from acquirers to issuers), then the current regulatory regime disadvantages the EFTPOS system.

Recently, EFTPOS Payments Australia Limited was established and a board of directors appointed. The purpose of this scheme is to enhance the competitive offerings of the EFTPOS product to customers and maximise its popularity with customers. By restricting EFTPOS Payments Australia in the range of business decisions it can take to pursue this objective, the regulatory anomaly potentially erodes competition.

The ABA welcomes the role that EFTPOS Payments Australia will play in setting interchange fees in the future. EFTPOS Payments Australia is well positioned as the appropriate forum for setting such fees.

The ABA's primary concern is related to the overall payments system and having the right structures in place to enhance competition. A consistent regulatory regime is an important step in this direction.

Ultimately, as argued previously, our view is that the best regulatory regime is that of full deregulation of interchange fees. This provides the most commercial freedom for participants to compete.

The ABA also notes that MasterCard Australia and Visa have undertaken considerable marketing and advertising in recent years to directly promote their debit products over EFTPOS. This suggests the international card schemes see it as a direct competitor, while at the same time, current regulatory restrictions limit EFTPOS' ability to respond.

Efficiency implication

To the extent that the current regulatory framework hinders EFTPOS in competing with scheme debit, then an efficiency implication arises.

The Reserve Bank's study on payment costs in Australia¹ gave some evidence that scheme debit is a more costly payment instrument than EFTPOS.

This provides some evidence that it is beneficial – from a cost and economic efficiency perspective – and from an economy-wide resource perspective, for customers to use EFTPOS over Scheme debit. Current regulation, curiously, works against this.

Although care needs to be taken in interpretation, the resource cost differential suggests there is considerable merit in aligning regulatory regimes of EFTPOS and scheme debit.

Access issues

¹ Carl Schwartz, Justin Fabo, Owen Bailey and Louise Carter, 'Payment Costs in Australia', available on the RBA website, www.rba.gov.au.

There is a potential concern that by changing the regulation of EFTPOS interchange, interchange fee negotiations could pose an access barrier. This arises whereby a new entrant's desire to enter the EFTPOS issuing or acquiring market could be impeded by existing players offering unfavourable interchange fees. To address this issue, the ABA would support EFTPOS Payments Australia Limited moving to multi-laterally agreed interchange fees – as discussed in the Reserve Bank's Consultation Paper.

The ABA does not believe that access will pose a problem in practice, particularly given that the newly established EFTPOS Payments Australia has a mandate to increase EFTPOS usage and popularity. Consistent with this mandate is increasing the number of institutions seeking to issue and acquire EFTPOS transactions. The ABA is confident this incentive will ultimately assist in encouraging new participation rather than hindering it, not dissimilar to the incentives operating in scheme debit.

Impact on retail pricing

A relevant question is whether any change in EFTPOS interchange, as a result of the proposed regulatory change, will impact retail pricing. The ABA's view is that given merchants and their representatives have often said that the savings from credit interchange fee reduction was too small to impact retail prices, then there would be no prospect that a small change in EFTPOS interchange would have any impact at all, including a reversal of the interchange fee direction.

This is because the impact of a small reversal of EFTPOS interchange would be insignificant compared to the large merchant savings generated by credit card reform.

As part of the RBA's proposed EFTPOS reform, we would support a regulatory impact statement which would ideally include an updated estimate of the extent to which merchants have directly benefited from retail payments reform initiatives.

The very substantial benefit that merchants have received in an almost halving of credit card interchange fee costs is a relevant contextual fact in Informing public debate on the proposed EFTPOS changes.

Sydney

23 October 2009