

UNSW Business School

New Payments Platform: Functionality and Access

Submission to RBA: 30 November 2018

Introduction

This short and non-confidential submission is made by Dr Rob Nicholls. I am a Senior Lecturer at the UNSW Business School.

I welcome the opportunity to make this submission to the Reserve Bank of Australia (**RBA**) on the New Payments Platform (**NPP**) Functionality and Access.

In my view, there should be two forms of access regime to the NPP and both should have clear pricing principles associated with them. This submission addresses these issues. The threshold issues as to whether there should be an access regime at all has already been dealt with by the Productivity Commission.¹ In addition, the NPP is a facility of national significance. As such, it meets the criteria for declaration set out in Part IIIA of the *Competition and Consumer Act 2010* (Cth). Summarised from s.44CA, these criteria are:

- (a) that access to the service, on reasonable terms and conditions ... would promote a material increase in competition in at least one market;
- (b) that the facility that is used to provide the service could meet the total foreseeable demand in the market;
- (c) the facility is of national significance; and
- (d) that access ... would promote the public interest.

It would be preferable if an access regime was offered by NPP and that the RBA facilitates the Payments System Board's management of that offer. The alternative path of declaration should be adopted by the Australian Competition and Consumer Commission (**ACCC**) if the RBA does not take this path.

On its consultation webpage, the RBA notes that "Osco is the only overlay service provided for the NPP. However, BPAY is planning on expanding Osco's services". What is unstated here is that BPAY is owned and controlled by the four major retail banks and does not have

¹ Productivity Commission (2018), 'Competition in the Australian Financial System', Inquiry Report No. 89, June, available at <<https://www.pc.gov.au/inquiries/completed/financial-system/report>>.

appropriate incentives to encourage innovation and competition with those banks by providing non-discriminatory access. This is precisely why an access regime is required.

Types of Access

As is common, I refer to the NPP service provider as the **access provider** and I refer to the person seeking to use the NPP as an **access seeker**.

There are broadly two types of access that should be provided to the NPP.

The first is access to overlay services. This is analogous to a Layer 3 access service in the telecommunications sector. Layer 3 provides connectivity between logical (as opposed to physical) points of interconnection. Access to overlay services will enable competitors to BPAY to emerge. It will also permit access for access seekers which are not Authorised Deposit-taking Institutions (**ADI**). It is likely that these non-ADI players will be FinTech service providers that will offer innovative applications of the data used by the NPP. This access to overlay services needs to be provided on a non-discriminatory basis. It is important to note that this non-discrimination applies not only as between access seekers, but in the provision of similar services to shareholders of NPP Australia Limited (**NPPA**).

The second is access to services requiring gateway interconnection. This is analogous to a Layer 2 access service in the telecommunications sector. Layer 2 provides connectivity between physical (as opposed to logical) points of interconnection. The points would be ports on the relevant gateway. Access to gateway services will facilitate competition from services providers that may become ADIs. It would be prudent to require, as a condition of access, that the access seeker does not use access to create money.²

The requirements for such an access regime would be consistent with usual practice associated with either essential facilities or bottlenecks in networked industries. However, there will need to be slight differences in the regime, depending on whether access is to an owned and operated gateway or to a third-party gateway that was required to be created as part of the regulation governing the NPP.

If the access provider has an owned and operated gateway, then the access provider must, if requested to do so by an access seeker:

- (a) supply access to the gateway to the access seeker;
- (b) take all reasonable steps to ensure that the technical and operational quality of the gateway supplied to the access seeker is equivalent to that which the access provider provides to itself; and

² Consistent with the speech by Christopher Kent on 19 September 2018 “Money – Born of Credit?” available at <<https://www.rba.gov.au/speeches/2018/sp-ag-2018-09-19.html>>.

- (c) take all reasonable steps to ensure that the access seeker receives, in relation to the gateway, fault detection, handling and rectification of a technical and operational quality and timing that is equivalent to that which the access provider provides to itself.

If the access provider has created a third-party gateway, then the access provider must, if requested to do so by an access seeker:

- (a) supply access to the gateway to the access seeker; and
- (b) take all reasonable steps to ensure that the access seeker receives, in relation to the gateway, equivalent technical, operational and data access outcomes to those which the access provider provides to itself.

Access pricing

The pricing of access should ensure that the access provider makes a normal return on its investment. This return is the weighted average cost of capital of the business. The RBA collects the debt/equity ratios of each of the NPPA shareholders. The RBA also knows the credit rating of each. The RBA determines the risk-free rate and is aware of the equity risk premium in Australia. It also knows that each of the banks offers fully franked dividends. As a consequence, the RBA knows the weighted average cost of capital of each of the NPPA shareholders. It would be reasonable to use a weighted average of these (weighted by market capitalisation) as a proxy for the weighted average cost of capital of NPPA.

For an overlay service, the access price should be equivalent to the price charged to other NPPA shareholders less the cost of selling that service to those NPPA shareholders. That is, the pricing for an overlay service should have a “retail minus retail costs avoided” construct. This has the benefit of encouraging entry and also promoting investment in gateway access, once a service has proved to be popular.

For a gateway service, the access price should be the long-run incremental cost of the gateway (using the weighted average cost of capital discussed above). In practice, for an existing gateway, this price will be vanishingly small until the transaction volume approaches the same order of number of transactions as the access provider. For a third-party gateway, the cost will be the relevant fraction of the cost of that gateway. This is also likely to be very small compared to transaction value.

It is essential that the access price should be comparable to the access cost of the access provider (at normal returns) in order to promote competition, innovation and entry.

Contact

I would be pleased to amplify the points made in this short submission. I can be contacted on 0412 646 477 or on r.nicholls@unsw.edu.au.