

Overview

The Payments System Board of the Reserve Bank was established over three years ago with a mandate to promote safety, efficiency and competition in the payments system in Australia. It has now been given additional responsibility for the safety of systems that clear and settle securities transactions in Australia's wholesale financial markets.

The focus on safety is a recognition of the importance of well-designed and smoothly functioning payments and settlements systems for the overall stability of the Australian financial system. Australia rates highly on safety matters – a judgment confirmed by the Board's assessment a year ago of Australia's compliance with emerging international norms in this area – and these matters have not become major agenda items for the Board. The broader mandate for efficiency and competition in the payments system is a recognition that Australia is not at international best practice and that existing market and governance arrangements are not an assured route to that goal. Not surprisingly, efficiency and competition issues have occupied most of the Board's attention over the past year and more.

In the retail payments area, the Board has concentrated particularly on the price incentives facing consumers of different payment services and on the strength of competition in providing these services. If consumers are to make well-informed choices and resources are to be allocated efficiently in the payments system, price incentives should reflect demand and relative cost conditions. The Board's initial stocktake of the Australian payments system identified some unusual features about the pricing of payment services, and these were investigated more fully in the study of interchange fees and conditions of entry in debit and credit card networks, undertaken in conjunction with the Australian Competition and Consumer Commission and published in October 2000. The study's conclusion, that competition in card networks is not working as it should, has provided the direction for the Board's subsequent work.

In 2001, a major milestone for the Board was its decision to endorse the use, for the first time, of the Bank's formal powers in the payments system. The Bank brought the credit card schemes in Australia under its regulatory

oversight and, after extensive consultation and detailed evaluation, it has now proposed a series of reform measures designed to promote greater efficiency, transparency and competition in the Australian payments system, to the benefit of the community as a whole. Underlying these reforms is the Bank's judgment that the restrictions that are imposed by credit card schemes and their members are not in the public interest and result in the community paying a higher cost for its retail payments system than is necessary. The Bank is using its payments system powers, not to regulate the credit card market, but to end the restrictions already in place that do not allow competitive forces to work. A further round of consultations with interested parties will take place before the Bank finalises the reform measures. These developments naturally take up the larger part of this Report.

Inadequacies in price incentives in ATM and debit card networks were also identified in the joint study and remain on the Board's agenda. These issues are yet to receive the same attention from industry participants as credit card reform but the Board welcomes the reviews which are now underway, which the Bank is helping to facilitate. The Board also remains committed to improving consumer safeguards in the use of the direct debit system. The Charter for Direct Debit Customers that

was developed with billing organisations, and published in last year's Report, was an important step forward but the Board also looks to financial institutions to play their part in promoting the use of this highly efficient payment instrument.

In the safety and stability area, the Board's main objective has been to prepare for the new responsibilities it has been given to ensure that securities clearing and settlement facilities conduct their affairs in a way that is consistent with financial system stability. The Bank's new standards-setting powers in this area are being developed in the context of an industry undergoing considerable rationalisation – a process that should provide a welcome boost to efficiency, given Australia's previously fragmented arrangements, but one that can lead to a concentration of financial and operational risks. The Bank's standards will be addressed particularly to these risks. Risk reduction is also the objective of a global initiative to develop a special-purpose bank – CLS Bank – to handle the settlement of foreign exchange transactions in major currencies, including the Australian dollar. This initiative has been underway since 1997 and, although the start-up date has now slipped well into 2002, the Board remains a strong supporter. The Australian market is now well-prepared for these new settlement arrangements.

