

Executive Summary

This Consultation Document sets out the Reserve Bank's draft standards for the EFTPOS and Visa Debit payment systems and the Bank's core reasoning underlying these proposed standards. The Bank is seeking submissions on the draft standards and its reasoning by 29 April 2005. Submissions will be published on the Bank's website.

Decisions on the final form of any standards, which will take into account submissions received, will not be taken by the Payments System Board until after the current Federal Court case, challenging designation of the EFTPOS system, has been decided. If warranted, the Bank will conduct further consultation after the determination of this case.

Three standards are proposed with the aim of improving competition and efficiency in the Australian payments system. The first two deal with interchange fees in the EFTPOS and Visa Debit systems, while the third deals with the 'honour all cards' rule in the Visa system and the so called 'no-surcharge' rule in the Visa Debit system.

In the Bank's opinion, current interchange fee arrangements in the EFTPOS and Visa Debit systems are not conducive to the efficient operation of the Australian payments system. In reaching this opinion, the Bank has considered not just the individual payment systems in isolation, but also the payments system as a whole. It has also considered how the system is likely to evolve over time, particularly given the current incentives facing merchants, financial institutions and cardholders.

The existing interchange fees in the EFTPOS and Visa Debit systems are subject to limited competition and appear not to have been set with the efficiency of the payments system in mind. In the EFTPOS system, fees are paid by the cardholder's bank to the merchant's bank, while in the Visa Debit system the reverse is the case. Moreover, the fee applying to Visa Debit transactions is the same as that applying to Visa credit card transactions, despite issuers of Visa Debit cards not providing the interest-free credit that is a feature of most credit cards.

An important effect of these interchange fees is that cardholders face higher prices for EFTPOS transactions than for credit card and Visa Debit transactions. This is despite the EFTPOS system having lower resource costs. This misalignment of relative prices and costs does not promote efficient payment choices by cardholders.

The high relative price of EFTPOS has contributed to the growth of the credit card system at the expense of the EFTPOS system. Further, should regulatory certainty be given to the current interchange fee arrangements, there would be a strong incentive for financial institutions to promote scheme-based debit systems, such as Visa Debit, at the expense of EFTPOS. To the extent that interchange fees mean that the higher-cost payment systems grow at the expense of the lower-cost EFTPOS system, merchants' payment costs rise and, thus, so too does the overall level of goods and services prices in Australia.

The proposed standards seek to bring relative prices and costs into closer alignment by narrowing the current differential in the interchange fees in the EFTPOS and Visa Debit systems. If the proposed standards were implemented, the maximum interchange fee in the EFTPOS system is likely to be around 5 cents paid to the merchant's bank. This compares with the current average fee of around 20 cents. In the Visa Debit system, the interchange fee paid to the cardholder's bank would fall from an average of around 40 cents to a maximum of around 15 cents. The combined effect of these proposed changes would be to reduce the gap between the interchange fees from around 60 cents at present to a maximum of around 20 cents.

Narrowing this gap would be expected to change the relative pricing of these two payment methods and/or the degree to which the two methods are promoted by financial institutions. The Bank's view is that, in time, such changes would affect the relative use of payment methods, including credit cards.

The Bank recognises that, if these standards were implemented, the benchmark interchange fees in the EFTPOS, Visa Debit and credit card systems would each be based on different eligible costs. To a significant extent this is the result of the interchange fees in the various schemes being so far apart initially and the Bank's desire to take an evolutionary, rather than revolutionary, approach to reform.

The Bank has already announced its intention to review the standards for the credit card schemes in 2007. At that time the Bank intends to review interchange fees in all card payment systems to assess whether the public interest would be promoted by moving the various arrangements for setting interchange fees to a more consistent basis.

In proposing these reforms it is not the Bank's intention to encourage the use of EFTPOS simply because of its lower relative costs. Rather it is the Bank's view that the efficiency of the overall payments system would be improved by cardholders being free to choose whatever payment instrument offers them the best value based on effective prices that more closely reflect relative costs than is now the case.

The third standard addresses the current requirement that merchants accepting Visa credit cards also accept Visa Debit cards. In the Bank's opinion this restriction limits normal competitive forces and impairs efficiency by requiring that merchants accept a payment instrument at a price which may be above the value that they receive from doing so. The proposed standard also formally applies the no-surcharge standard to the Visa Debit scheme. The Bank expects that similar arrangements would apply to other scheme-based debit arrangements that might be introduced in Australia.

The Bank has also considered access arrangements in the EFTPOS system. While the draft regime being developed by Australian Payments Clearing Association (APCA) represents an improvement on existing arrangements, the Bank has recently written to APCA raising a number of issues with the proposal. If these issues are not addressed satisfactorily, and in a timely manner, the Bank will consider issuing a draft access regime for public comment.