

Submission to the Reserve Bank of Australia

Designation of EFTPOS

15 October 2004

1. Introduction

Background

The Payments System Board of the Reserve Bank of Australia (RBA) decided to designate the EFTPOS payment system on 9 September 2004. This designation is intended to cover the setting of EFTPOS interchange fees, but not EFTPOS access, according to the RBA media release. The RBA had previously designated the Visa Debit payment system on 23 February 2004.

According to the RBA media release:

“The Bank will now proceed to consider the desirability of setting standards for interchange fees for both the EFTPOS debit card payment system and the Visa Debit payment system with the objective of improving the efficiency of Australia’s payments system.

The Bank will take into consideration any further submissions on these matters by interested parties.”

This submission from the Australian Merchant Payments Forum (AMPF) is in response to this invitation.

Objective

The objective of this submission is to demonstrate why a standard for setting EFTPOS interchange fees is not in the public interest and therefore is not desirable.

2. Designation of the EFTPOS Payment System

The AMPF does not accept that there were any valid grounds to designate the EFTPOS Payment System.

On 16 September 2004 the AMPF made a request pursuant to section 13 of *Administrative Decisions (Judicial Review) Act 1997* to the RBA to furnish a statement in writing setting out the RBA's findings on material questions of fact, referring to the evidence or other material on which those findings were based, and giving the reasons for the decision.

On 21 September 2004 the AMPF requested the RBA, in light of its request for information, to extend the time for the lodging of these submissions to a period of five weeks after that information had been received. AMPF advised that it would be unable to make any substantive submissions concerning the desirability of setting standards for interchange fees in the absence of this information. This request has been declined by the RBA.

The RBA did not provide reasons for its decision to designate the EFTPOS payment system until 14 October 2004, the day before these submissions were required to be provided to the RBA, and the AMPF has not had an opportunity to give proper consideration to them.

The AMPF makes these submissions without the benefit of proper consideration of the information provided by the RBA, and without prejudice to its rights under the *Administrative Decision (Judicial Review) Act* in relation to the RBA's decision to designate the EFTPOS payment system.

It is likely that the AMPF will make further submissions once it has given due consideration to the RBA's reasons for its decision.

3. Standard for EFTPOS Interchange Fee Not in the Public Interest

Having designated the EFTPOS payments system, the RBA may impose standards to be complied with by participants in the system under s.18 of the PSRA only if it considers that that action is in the public interest.

Public interest is defined in s.8 to include matters relating to prudential security of the payment system, efficiency and competition.

The AMPF notes that the RBA, in its press release dated 9 September 2004, explained that it had concluded:

- “that current interchange arrangements are not conducive to the efficiency of the overall payments system”
- “the nature of the interchange arrangements contribute to the effective price that cardholders are charged for payments using EFTPOS being higher than for payments using credit cards”
- “this is despite the EFTPOS system having relatively lower costs”
- “a narrowing of this differential in relative prices and costs would promote the efficiency of the overall payments system”

Accordingly, it appears that the RBA is of the view that regulating the EFTPOS interchange fee to reduce the fee will lower EFTPOS transaction costs to cardholders, resulting in an increase in EFTPOS usage in particular at the expense of credit card usage, and this will in turn increase the efficiency of the overall payment system, and thereby promote the public interest within the meaning of s.8.

As the RBA is aware, the Australian Competition Tribunal, in *Re EFTPOS Interchange Fees Agreement* [2004] CompT7 (25 May 2004) thoroughly examined and rejected all four propositions in the press release set out above.

The major banks, in their application for authorisation of an agreement fixing the interchange fee at zero, argued before the Australian Competition Tribunal (supported by the RBA) that reducing the interchange fee to zero would increase the efficiency of the overall payment system [at paras 27 and 148].

The Tribunal considered 711 pages of witness statements, heard that evidence tested in cross examination over four sitting days as recorded in 548 pages of transcript, considered 360 pages of written submissions from all parties including 78 pages of submissions from the RBA, and heard oral submissions over three sitting days recorded in 239 pages of transcript, including submissions from the RBA. The Tribunal concluded that the imposition of a zero interchange fee would result in detriments that clearly outweighed any benefits [153] and accordingly was not in the public interest.

More particularly, the Tribunal found that:

- the proposition that encouraging greater use of EFTPOS at the expense of credit cards promoted efficiency should be rejected [151];
- credit cards provided benefits to cardholders not available to holders of debit cards [61];
- encouraging a switch from credit cards to debit cards is not warranted on allocative efficiency grounds. They are simply different products [155];
- the extra costs identified in the Joint Study [between credit card transactions and debit card transactions] are incurred because of the difference in the characteristics of the [two products] [150];

- the proposition that there were distorted price signals between credit cards and debit cards was not established [149];
- there is a very high level of EFTPOS users who under current arrangements pay no fees anyway [118];
- an offer of additional free EFTPOS transactions to a person [with no available funds] would not increase their use of EFTPOS [118]; and
- any pass through by issuers of the savings as a consequence of any reduction in the interchange fee would be small, may take the form of other adjustments to the complex bundle of bank charges, and is not likely to be conduct altering [115].

The Tribunal also found that a reduction of the interchange fee from its current level (being a level set in a free market environment) to zero was likely to result in significant detriments, including:

- a general increase in the price for goods and services [130 and 134];
- a passing to the general body of consumers of costs which are currently incurred within the banking system [157];

and the increased cost to merchants was likely to operate as a disincentive to undertake future investment in the upgrading of the EFTPOS system [135].

Since the Competition Tribunal decision in May 2004, there has been an increase in the number of EFTPOS fee-free transactions offered by the Banks, as they respond to competitive pressure.

A recent survey of bank websites reveals that the number of 'fee free' accounts is growing rapidly. A number of financial institutions now offer transaction accounts to their customers which include unlimited EFTPOS transactions, with no transaction fees payable. These accounts include:

- ANZ Bank – Access Advantage account;
- National Australia Bank – Smart Direct account; and
- Westpac Bank – Westpac One account.

It is a well accepted principle of economic regulation that regulation should only be imposed on commercial behaviour within a free market environment in circumstances of clear market failure, and where the benefits of regulation will outweigh the costs.

The AMPF submits that no case has ever been demonstrated for regulatory intervention in the setting of EFTPOS interchange fees, which are currently set in a free market environment. It is very clear that the market is delivering reduced EFTPOS transaction fees. As the RBA's stated objective is to reduce these fees, and as the market is delivering that outcome, it is beyond doubt that regulatory intervention through the setting of standards for EFTPOS interchange is not necessary, is not desirable, and is not in the public interest.

As noted in Section 2, the AMPF is currently reviewing the RBA's *Reasons for the decision to designate the EFTPOS payment system* dated yesterday, 14 October 2004, and will be making further submissions once that analysis has been completed.

4. Visa Debit

Visa Debit cards offer cardholders no more benefits at the point of sale than do EFTPOS cards. Therefore, no distinction should be drawn between the treatment of Visa Debit and other debit cards in relation to interchange fees.

Merchants who accept Visa Credit cards are currently compelled by the Honour All Cards Rule (HACR) to accept Visa Debit. In addition Visa Debit cards cannot be distinguished visually or technologically from Visa Credit cards, so merchants who are happy to accept Visa Credit cards, but would prefer not to accept Visa Debit cards, are unable to do so.

If Visa is unwilling to remove the HACR as it applies to different products, and to distinguish Visa Debit from Visa Credit visually and technologically, a standard should be set to compel it to do so.