

12 October 2006

Dr John Veale
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By email to: pysubmissions@rba.gov.au

Dear Dr Veale

2007/08 Review of Reforms to Card Payment Systems

I refer to the Reserve Bank of Australia (RBA) Media Release of 13 September 2006 (Update on Payments Systems Issues) where the RBA, inter-alia, sought the views of interested parties on the content and process of the above mentioned review.

The Commonwealth Bank (the Bank) appreciates the opportunity to contribute to the RBA's formative thinking on this important review. We also appreciate the fact that RBA is considering issues surrounding this review so far in advance of its commencement – we believe this reflects both the importance of this review and its likely complexity. The RBA, and industry participants, now have the opportunity to try to optimally position the review (in terms of both content and process).

As you are well aware, the Bank has been a long and active participant in the reform debate over recent years, and we look forward to this tradition continuing, as we strive to be Australia's leading financial services organisation, and as we fulfill our responsibilities as a key participant within the broader payments industry.

We note that the RBA Media Release refers to a

“review of the reforms to card payment systems, including interchange fees ...”.

The Bank is of the view that the forthcoming 2007/08 review provides an ideal opportunity for the RBA to adopt a broader purview, and instead of focusing solely on card payment systems, should incorporate at least elements of other payment systems. It occurs to the Bank that a study of “Cash” – particularly in relation to the cost and pricing thereof would, for example, provide a useful benchmark for evaluating recent card based reforms.

We note also that the review will “include” interchange fees. We take this to mean that broader elements will also be addressed – such as “access” and competitive impacts (especially in relation to three party card systems).

We also take the “reform” element to refer to the regulatory intervention introduced by the RBA dating back to immediately following the RBA / ACCC Joint Study.

Under the Payment Systems Regulation Act, the RBA must have regard to competition and efficiency consequences of its actions. We assume that will be the case under the review process.

Turning to the two specific aspects upon which you have sought views, ie “*content*” and “*process*” of the review.

Content

In relation to the “content” of the review:

- As discussed above, we believe that the review should have a broader content than that initially suggested in the 13 September Media Release.
- We believe that the case needs to be made to justify ongoing intervention – to identify the ongoing market failure giving rise to a loss of social welfare (greater than the cost of ongoing regulation) and thus warranting ongoing intervention. Also, the precise nature of the factors giving rise to the market failure should be unambiguously identified and articulated.
- Similarly, the review should indicate how the current regulations have addressed the problems perceived at the time of promulgating Standard Number 1 and subsequent Standards.
- We believe that the content of the review must be such as to include a review of the “success” of the RBA’s reforms introduced since the early 2000’s. Measurement of “success” should be approached broadly. It is unfortunate that criteria for “success” were not articulated when the RBA first intervened in the Credit Card market prior to publication of Standard Number 1.
- Further, as part of the “success” evaluation, end market impacts should be explicitly studied – seeking to clearly identify “winners” and “losers” and potentially disparate outcomes – for cardholders, retailers, issuers, acquirers, processors etc. Areas such as innovation, investment, the degree to which impacts have been passed to end markets, and the competitive dynamics of the market, and other related markets, warrant attention.
- Further to the above point, we would be keen to see explicit consideration of competitive neutrality concerns in relation to “three party” card schemes.
- This review also provides an opportunity for the RBA to publish a complete statistical review of data collected under the reform process – bringing together into “one place”, a time series of data spanning the reform period which is currently published in a number of different locations. This would be a useful reference tool for the industry.
- A review of the appropriateness of a cost based approach to interchange fee setting, as opposed to other measures that sought to recognize value or benefits, would also be a useful contributor to this review.
- The costs of regulatory intervention – again from a broad perspective – and as incurred by all stakeholders, would also usefully inform debate in this area.

Process

In relation to the review “process”:

- We believe that the process of the review should be as open and transparent as possible, bearing in mind the confidentiality constraints imposed on the RBA. Preservation of confidentiality assurances remains vital.
- The review should, in our view, be collaborative and consultative – involving feedback, discussion, publication of working papers etc – and providing sufficient time for meaningful consideration, review and discussion and genuine consultation and comment on what are likely to be complex matters.
- All discussion documents issued by RBA should be placed on the public record; similarly, all submissions from interested parties should automatically be put on the public record (except for those parts of the submissions where the originating party can justify suppression on *legitimate* commercial-in-confidence grounds).

- Consultation with a broad group of interested parties is also vital, we believe, to the success of this review. Representative bodies such as the Australian Bankers' Association (ABA) or the Australian Payments Clearing Association can frequently add value to reviews such as these. In the past, RBA has not always been receptive to the inclusion of such representative bodies, preferring to deal directly with participants. We believe that both direct and representative consultation will prove beneficial.
- The use of independent experts would also be a useful approach to be considered by the RBA. This is not to question the RBA's analytical ability, but introducing a strong element of independence would remove potential accusations of bias as the RBA reflects on its own reforms.

Other Aspects

At the core of the above discussion is a "cost / benefit" analysis of the RBA's recent regulatory interventions – seeking to identify clear costs and benefits to assist form the view as to the ultimate "value" of intervention, and as a guide to future intervention.

It also occurs to us that the "Principles and Guidelines for National Standard Setting and Regulatory Action by Ministerial Councils and Standard – Setting Bodies" (as endorsed in April 1995 by the Council of Australian Governments [COAG]), provide useful guidance to the evaluation of regulatory impact. Without presenting a lengthy review of that document, some pertinent elements arise that could usefully be applied to the forthcoming review, such as:

- Assessment of the need for regulation;
- Identification of any regulatory failure (and identification of the market failure warranting regulation in the first place; and thus justifying ongoing regulation);
- Alternative solutions (to ongoing regulation);
- Benefits / Costs and quantitative (including risk) assessments;
- Minimising the impact of regulation – including administrative burdens;
- Minimising the impact on competition;
- Predictability of outcomes, and assessment of secondary effects; and
- Accountability (by the regulator).

The above list does not claim to be an exhaustive appraisal of the lengthy COAG document, but we take this opportunity to suggest that the RBA might consider adopting elements of the above framework as a way in which to review and evaluate recent regulatory interventions.

We are also aware of the intention of the ABA to lodge a submission on this topic. We are supportive of the points being raised in that submission.

We thank you again for the opportunity to lodge this submission. The Bank remains ready and willing to discuss any of the above points, and to that end, please contact the writer on (02) 9312-7523.

Yours sincerely

[Signed]

Stuart Woodward
General Manager
Industry and Alliance Management