



Abacus
Australian Mutuals

Association of Building Societies and Credit Unions

30 October 2009

Mrs Michele Bullock
Head of Payments Policy
Payments Policy Department
Reserve Bank of Australia
pysubmissions@rba.gov.au

Dear Michele,

Consultation on proposed changes to the EFTPOS interchange fee standard

Abacus – Australian Mutuals supports the RBA's proposed changes to the EFTPOS interchange fee standard and suggests some enhancements to further promote competition between EFTPOS and scheme debit.

We note the RBA's statement that "the change does not imply that interchange fees in the different systems should be equal, only that they are subject to equivalent regulation."

Our suggested enhancements to the new EFTPOS interchange fee standard are:

- a floor of zero in addition to the proposed "cap on weighted-average interchange fees of 12 cents per transaction"; and
- inclusion of EFTPOS cash-out transactions.

Mutual ADI sector

Abacus is the industry association for credit unions, mutual building societies and friendly societies.

Credit unions and mutual building societies are Authorised Deposit-taking Institutions (ADIs) under *Banking Act 1959* and provide banking services to 4.5 million Australians. Mutual ADIs provide their members with highly competitive banking products and services, including EFTPOS debit cards, scheme debit cards and credit cards.

Mutual ADIs strongly and consistently outperform the major banks in independent customer satisfaction surveys. The new Mutual Banking Code of Practice makes 10 key promises including: We will be fair and ethical in our dealings with you; We will focus on our members; and, We will deliver high customer service and standards.

The mutual ADI sector has 11.6 per cent of the household deposits market (more than NAB and slightly less than ANZ) and a growing share, currently 8.1 per cent, of the new owner-occupier home loan market.

The ACCC has described credit unions and building societies as "strong competitors on customer service", with a 17 per cent share of transaction accounts in the NSW/ACT market and 24 per cent share in the SA market.¹

EFTPOS and scheme debit

Abacus supports the objective of a competitive market in debit card products. Constraints on the capacity of EFTPOS debit to compete with Visa Debit and MasterCard Debit should be removed.

EFTPOS will always be at a disadvantage to scheme debit if issuers have to pay, rather than earn, interchange fees.

Credit unions and building societies have been strong supporters of both EFTPOS debit and scheme debit for many years. The Visa Debit card was launched in 1982 by credit unions and building societies. Credit unions were able to access the EFTPOS system from 1985.

Major banks have become supporters of scheme debit in very recent times and, along with the schemes, have been actively promoting scheme debit leading to recent strong growth of scheme debit.

The Payments System Board 2009 annual report says the value of scheme debit purchases increased by 35 per cent over the year to the June 2009 quarter, compared with a 12 per cent increase in the value of EFTPOS transactions. "Scheme debit accounted for around one-quarter of the value of debit card payments in the June quarter of 2009, compared with a share of around one-fifth a year earlier," the PSB said.

It appears that scheme debit is rapidly overtaking EFTPOS debit, indicating that measures to level the playing field are now urgent.

Scheme debit already has the significant advantage of card-not-present functionality (i.e. transactions online, telephone & mail) and now matches EFTPOS debit's security factor of PIN authorisation. EFTPOS, temporarily, has the advantage of cash-out functionality but this is also likely to be matched by scheme debit.

Resistance to reform of interchange fees for EFTPOS debit has been led by large merchants ever since the RBA and the ACCC found in their joint study on the payments system 10 years ago that:

"The payment of a debit card interchange fee to acquirers is an arrangement unique to Australia. In other countries, the payment is to the card issuer or there are no interchange fees at all."²

¹ Statement of Issues – WBC proposed acquisition of St George. ACCC 23 July 2008.

² DEBIT AND CREDIT CARD SCHEMES IN AUSTRALIA - A STUDY OF INTERCHANGE FEES AND ACCESS. RBA/ACCC. OCTOBER 2000

Since then, the RBA's reforms to credit card interchange fees have delivered billions of dollars in benefits to merchants and billions of dollars in additional costs to cardholders.

The PSB annual report says the aggregate net savings to merchants over 2008-09 alone from declines in merchant service fees is estimated at \$1.2 billion.

The RBA's reform allowing merchants to impose surcharges on cardholders continues to be enthusiastically embraced. The PSB annual report quotes data saying there has been strong growth in surcharging by merchants in recent years and that strong growth in surcharging will continue.

The RBA's reforms have also pushed up cardholder fees and reduced the value of cardholder rewards programs. MasterCard calculates that cardholders are paying almost \$1 billion more per annum in additional fees and interest due to the regulatory intervention.³

Merchants have been clear beneficiaries to date of the RBA's payments system reforms. Issuers of credit cards and scheme debit cards have had interchange fee revenue massively reduced. EFTPOS card issuers have had the benefit of a reduction in the fees they pay to acquirers, but they continue to pay between 4 and 5 cents for purchase transactions and unregulated fees for 'cash out' transactions.

Floor of zero

The current EFTPOS interchange fee standard of 4 to 5 cents paid to the acquirer continues the "negative" interchange fee model that puts EFTPOS debit at a fundamental disadvantage to scheme debit.

It reduces the capacity of issuers to promote EFTPOS debit and it affects pricing to EFTPOS debit cardholders.

The new standard should be absolutely clear that "negative" interchange fees will no longer be a factor for issuers in their consideration of competing debit card products. Imposing a zero floor to the interchange fee range would also remove the risk of current EFTPOS issuers being worse off after the implementation of the new standard. The current standard has a cap and a floor.

Include cash out

Excluding cash out transactions from the EFTPOS interchange fee standard creates an additional layer of complexity in moving to new interchange fee settings.

It is an additional barrier to reform of a system that has been characterised by rigidities and inertia. It is also a barrier to entry into the EFTPOS market for new issuers.

The current exclusion of these transactions is based on a threat by merchants to cease providing cash out should their "compensation" via EFTPOS interchange fees be reduced.

³ MasterCard submission to RBA 23 October 2009

This claim is implausible given that cash out is a benefit to merchants because it reduces their costs of holding cash.

Merchants are highly likely to continue to provide cash out as a customer service and to reduce their own costs regardless of the regulatory treatment of EFTPOS interchange fees.

There is no longer any comparison to be made with the regulatory treatment of ATM interchange fees since the introduction this year of ATM direct charging.

Conclusion

The formation earlier this year of EFTPOS Payments Australia Limited (EPAL) to manage and promote the EFTPOS debit system was a crucial step in unleashing EFTPOS to compete effectively with Visa and MasterCard.

Abacus urges the RBA to ensure that the regulatory settings governing interchange fees enable EPAL to compete on a level playing field.

EPAL's 14 initial members include two entities, Coles Group and Woolworths, that have consistently opposed EFTPOS reform.

Given this internal challenge for EPAL, and the formidable competitive strength of the global card schemes, Abacus recommends that the RBA's implementation of its EFTPOS reform proposal should include a strong signal to stakeholders about the urgency and direction of the reform agenda.

Please contact me on 02 8299 9036 or Luke Lawler on 02 6232 6666 should you wish to discuss any aspect of this submission.

Yours sincerely,



LOUISE PETSCHLER
Chief Executive Officer