

INTERCHANGE FEES

Douglas Swansson, Coles Group

Good afternoon. My name is Douglas Swansson. I am the Group Manger for Payment Services for the Coles Group. I would like to thank the RBA for this opportunity to address you all today, and to be able to provide a retailers perspective on payments reform and more specifically on the issue of interchange fees.

Let me start by saying that we fully support the underlying principles that have been at the heart of the RBA's reform agenda namely transparency, efficiency and competition. These principles we believe are key to ensuring that we have a payments system that ensures low cost, efficient payment instruments thrive at the expense of less efficient ones.

Fundamentally this boils done to the issue of price signals and the relative pricing of payment instruments. Which brings me to today's topic of discussion – interchange fees.

Interchange fees have been the subject of much debate the world over, they have been the subject of litigation both here and overseas and have attracted the interest of central banks and competition authorities.

The reason is simple in our view. Interchange fees are a subsidy that distort the pricing of payment instruments and in turn their usage and acceptance costs for merchants.

In our view interchange fees are an unnecessary distortion and lead to inefficiencies or as Alan Frankel has explained "exploit externalities rather than solve them".

We support the AMPF's position that there is no justification for interchange fees and that they should be abolished. I appreciate that this not a position that we have always held at least with respect to EFTPOS debit, and to be clear we would not support the removal of EFTPOS debit card interchange fees in isolation.

It is with an opportunity to reflect over the past few years, and with a view to the fundamental principles outlined in the RBA's issues paper that we have come to this position.

The key question for us is what justification do we have for interchange fees being used to subsidise one parties costs over another. In relation to scheme cards why are issuers costs for authorisation, processing, interest free periods and fraud subsidised by merchants via an interchange fee?

These are not costs that merchants can influence or control and ultimately theses costs are borne by all consumers not just the scheme cardholders as they are passed on in the pricing of goods and services.

We would argue that the principle of user pays should apply, otherwise it is difficult to see how consumers can be presented with clear pricing signals for these payment instruments.

In our view looking forward, what is needed is a simple and transparent system where these hidden cross-subsidies are removed.

It is argued by some that card payments systems will not survive without interchange, that there is something inherently different about card payment systems from other payment instruments that have and continue to operate without the need of interchange fees.

Further it was claimed that the mandated reductions in credit card interchange fees introduced as part of the RBA's reforms in 2003 would lead to a "death spiral". Clearly this has not been our experience.

That said the reduction of this cross-subsidy has obviously lead to increased fees for credit cardholders, but this is exactly the point. A greater proportion of the costs of providing these payment instruments are now priced into the products that issuers offer to their customers.

It has also been argued that reduced interchange fees would hinder innovation, again this has not been our experience. We have seen for example significant developments in prepaid and gift cards, low interest rate credit card products, MasterCard scheme debit, contactless, PIN on credit, 3DES, near field communications, and chip cards.

I understand that the issue of innovation will be discussed in more detail later this afternoon.

Another issue relevant to interchange fees that has been raised is the question of whether changes such as the removal of the no-surcharge rule and the honour-all-cards rule have themselves adequately addressed our concerns.

To be clear the no-surcharge rule and the honour-all-cards rule we believe were unjustified commercial restrictions on our business that have restricted competition. We supported their removal and continue to do so.

As to whether these reforms alone are sufficient to address our concerns regarding interchange fees our answer is clearly no.

It is somewhat ironic that those who argued that the no-surcharge rule should not be removed, now offer it as a potential solution to the concerns we have expressed about interchange fees and their impact on pricing signals.

Whilst the adoption of surcharging has increased since the removal of the no-surcharge rule, it is by no means widespread and we believe there will always be barriers to its adoption by some merchants for a number of valid reasons, such as the costs to develop systems and processes to collect these surcharges and competitive pressures within the retailing industry.

But why should merchants be expected to address these hidden cross-subsidies, is this not a case of treating the symptoms not the cause. We feel that this is a distraction from the key issue namely what is the justification for interchange fees in the first place.

To summarise then, we advocate a move to eliminate interchange fees to remove unnecessary and unjustified cross-subsidies. We support a continuation of the abolition of the no-surcharge rule and the honour-all-cards rule.

Overall we believe that that RBA's intervention on interchange fees has been beneficial to the Australian public and we urge that it continues moving forward with its reforms.

Thank you.