3. Retail Payments Regulation and Policy Issues

The Reserve Bank determines policy for, and undertakes research into, retail payment systems under its remit to promote a safe, competitive and efficient payments system. Recent policy work has focused on concluding the Bank's comprehensive Review of Retail Payments Regulation, which commenced in late 2019. With the ongoing transition away from cash and towards electronic payments, the Bank has continued to examine whether there are any policy issues regarding access to cash services, as well as the cost, reliability and security of electronic payment services. The importance of this work has been underscored by the changes in payment behaviour stemming from the COVID-19 pandemic. The Bank continues to monitor the rapid pace of innovation in the payments system and changes in market structure, and has considered a number of policy and regulatory issues associated with new players and innovations in the payments system throughout 2020/21.

Review of Retail Payments Regulation

The Bank commenced a comprehensive Review of Retail Payments Regulation with the publication of an Issues Paper in November 2019.[1] The Review was put on hold for much of 2020 to reduce the demands on industry stakeholders during the COVID-19 pandemic.

In May, the Bank published a Consultation Paper, which set out the preliminary conclusions and proposed policy actions of the Board, together with draft variations to the Bank's standards for card payment systems.[2] The Bank received over 30 written submissions in response to the Consultation Paper and consulted with a wide range of interested parties over the course of the Review.

At the time of writing, the Bank was in the late stages of the Review after considering the feedback and was expecting to publish the Board's final conclusions and variations to the standards in a Conclusions Paper in late October. The Review has addressed a range of payments policy issues, including: how to support dual-network debit card (DNDC) issuance and the provision of least-cost routing (LCR); the levels of the interchange fee benchmarks; scheme fee transparency; and the 'no-surcharge' rules of 'buy now, pay later' providers. These issues are discussed at length in the documents produced by the Bank for the Review.

Compliance with the Bank's card regulations

Interchange fees

Interchange fees are wholesale fees set by card schemes that are paid by the merchant's bank

[1] See RBA (2019), 'Review of Retail Payments Regulation: Issues Paper', November.

[2] See RBA (2021), 'Review of Retail Payments Regulation: Consultation Paper', May.

(acquirer) to the cardholder's bank (issuer) on each card transaction. These fees affect the prices faced by cardholders and merchants for making and accepting card payments. The Bank's interchange standards cap the level of interchange fees that designated schemes can set for transactions using Australian-issued cards. Weighted-average interchange fees are required to be at or below a benchmark of 0.50 per cent for credit cards, and 8 cents for debit and prepaid cards. The weighted-average benchmarks provide flexibility to the schemes to set different rates for different card, transaction and merchant types. The benchmarks are supplemented by ceilings on individual interchange rates to limit the disparity between fees applicable to larger 'strategic' merchants and smaller businesses. These ceilings are: 0.80 per cent for credit cards; and 15 cents, or 0.20 per cent if the interchange fee is specified in percentage terms, for debit and prepaid cards.

Compliance with the interchange benchmarks is observed quarterly, based on transactions in the preceding four quarters. In the event that a scheme has exceeded the relevant benchmark, it must reset its interchange fee schedule, such that the benchmark would not have been exceeded if the new fees had applied over the preceding four quarters.

In recent years, the international schemes had typically set their interchange fees on credit cards such that the weighted-average fee was very close to the benchmark, resulting in frequent resets to their schedules. However, in 2020/21, interchange fees for both the Visa and Mastercard credit schemes remained at or below the credit interchange benchmark in each quarterly reporting period, and thus no resets were required. Even so, the schemes made a number of voluntary changes to their credit interchange fee schedules during the year, primarily to raise fees on some premium card categories.

Weighted-average interchange fees for debit and prepaid cards were also below the benchmark for all designated schemes during 2020/21. These fees have generally drifted down over the past few years in response to competitive pressures from LCR, and they declined a little further over the past year. Eftpos made a number of significant changes to its debit interchange schedule during the year, including the introduction of new 'package rate' categories with lower fees for merchants that choose to route DNDC transactions through the eftpos network. Visa and Mastercard introduced additional strategic merchant categories, with Visa also adding new, higher-fee categories for transactions on single-network debit cards, which cannot be routed.

Net compensation

To prevent circumvention of the interchange fee caps and benchmarks, the Bank's interchange standards contain a requirement that issuers may not receive 'net compensation' from a scheme in relation to card transactions. This requirement is intended to limit the possibility of schemes using payments and other incentives to issuers (funded by higher scheme fees on acquirers) to effectively replicate interchange fee payments. Schemes and issuers certify their compliance with this requirement annually. The certification process for 2020/21 indicated that the net compensation provision was working as intended. However, the reduction in cross-border card transactions associated with the COVID-19 pandemic resulted in a significant decline in scheme fees, and presented compliance challenges for some issuers.

In response to questions that arose during the previous compliance review, the Bank published guidance in February that sets out when the Bank expects new card issuers to first certify compliance with the net compensation provision. The guidance is expected to support new issuers' compliance positions while they are in the early stages of developing and launching a card product.

Surcharging

The Bank's surcharging standard protects the right of merchants to impose a surcharge on card payments from designated schemes, which helps promote competition in the payments system and keeps downward pressure on payment costs for businesses. However, to ensure that consumers are not excessively surcharged, the amount of any surcharge is limited to the merchant's average cost of accepting a card payment for the relevant scheme. Acquirers and payment facilitators are required to give merchants statements that clearly set out the average cost of acceptance for each designated card scheme, to help merchants make informed decisions about surcharging. These requirements are complemented by the Australian Competition and Consumer Commission's (ACCC) powers to monitor and enforce the ban on excessive surcharging. While the surcharging standard only applies to designated card schemes, a number of schemes and other payment providers that are not designated have provided the Bank with formal undertakings to keep their surcharging rules consistent with the standard.

The Bank's monitoring indicates that there has been a high level of compliance with the surcharging framework by schemes and acquirers. Further, the ACCC has indicated that there was a reduction in the number of complaints of excessive surcharging it received over the past year; although, in July a large corporate group paid penalties after the ACCC issued it with 12 infringement notices following an investigation into alleged excessive surcharging. In response to a number of queries prompted by some stores going cashless, the ACCC recently published guidance for businesses on how they should display prices for their goods or services, including the minimum card payment surcharge payable.[3]

Treasury Payments System Review

In October 2020, the Australian Government launched a review of the governance and regulatory arrangements for the Australian payments system, led by Scott Farrell and supported by a secretariat located within Treasury. The primary aim of the review was to ensure that the regulatory architecture and governance structures for the payments system remained capable of achieving their objectives and supporting continued innovation and competition in the market for payment services.

The Bank provided a written submission to the review and Bank staff engaged with Mr Farrell and the Treasury secretariat a number of times during the review. In its submission, the Bank noted that the existing regulatory arrangements for the payments system in Australia have worked well; they have helped shape a payments system that in most regards is providing high-quality services for Australian consumers, businesses and government entities. However, key aspects of the regulatory architecture have been in place for more than two decades and numerous changes have occurred in the payments system over that time or are underway. In this context, the Bank's submission raised a number of issues, including in relation to:

- overcoming the coordination challenges that can hold back system-level innovation in payment networks
- ensuring that the scope of regulation is appropriate to respond to the increasing range of entities that are now involved in the provision of payment services

[3] ACCC, 'Payment Surcharges'. Available at <https://www.accc.gov.au/business/pricing-surcharging/payment-surcharges#applying-a-surcharge-to-all-kinds-of-card-payments>.

- ensuring that industry self-regulatory arrangements support competition and innovation from new players, while appropriately dealing with the risks to other payments system participants and users
- exploring whether a specialised licensing and oversight regime for non-bank payment service providers could help promote access and competition while appropriately controlling risk
- clarifying the Bank's ability to set regulatory requirements to promote the financial and operational resilience of payment systems
- examining whether there are aspects of the regulatory regime and market practices that are currently limiting competition by non-bank participants in the market for cross-border payment services and international money transfers
- ensuring that the decline, and eventual closure, of legacy payment systems (such as cheques) is carefully managed to support the needs of users while promoting payments system efficiency.

The final report of the Payments System Review was released by the Treasurer in August 2021. The report concluded there have been significant changes in the payments ecosystem since the current regulatory architecture was established more than two decades ago. Participants in the payments ecosystem have grown in number and variety, and incumbents are changing the way they operate in response to evolving consumer preferences and technological developments. The report makes several recommendations to ensure that the payments system regulatory architecture and governance arrangements are fit-for-purpose for the years to come. These include:

- a greater role for the government, through the Treasurer, in setting the strategic direction of the payments ecosystem in collaboration with regulators and industry
- the development of a strategic plan for the payments ecosystem, supported by the introduction of a payments industry convenor and an enhanced payments function within Treasury
- greater coordination between payments regulators to ensure alignment with the agreed strategic direction
- expanding the scope of the Bank's designation power in the Payment Systems (Regulation) Act 1998 to ensure that the Bank can regulate new and emerging payment systems and introducing a new designation power for the Treasurer based on national interest concerns
- introducing a single, tiered payments licensing framework that replaces the need for providers to obtain multiple authorisations from different regulators, provides clear protections for consumers and businesses, and facilitates more transparent access to payment systems.

Treasury is currently consulting on the recommendations in the report ahead of the Australian Government finalising a response, which it plans to do before the end of the year. The Bank will continue to engage with Treasury and the Australian Government on this review and will respond to any recommendations on the Bank's regulatory framework supported by the government.

Innovation in payments and the digital economy

The Bank devotes significant resources to understanding the evolving structure of the payments system, in order to promote innovation and foster improvements in services for the benefit of households, businesses and government entities.

During 2020/21, Bank staff held numerous discussions with industry participants on new technologies and other factors that are driving innovation in the payments system and enabling new business models, as well as opportunities and challenges faced by newer entrants. The Bank also made two submissions to the Senate Select Committee on Australia as a Technology and Financial Centre.[4] These submissions focused on the potential role and implications of: central bank digital currency (CBDC), cryptocurrencies and digital assets; de-banking and access to payments infrastructure; and neobanks (see below for further discussion of the Bank's policy work in some of these areas).

Bigtechs such as Google, Apple, Facebook and Amazon are becoming increasingly involved in the global payments industry, including by providing various consumer payment services such as digital wallets. The Board discussed the role of bigtechs in payments during the year, recognising that these firms have the potential to promote a more efficient payments system by delivering new and innovative services. However, these platforms have large user bases and benefit from substantial network effects, which is likely to put them in a strong competitive position relative to other payment system participants. The involvement of large global technology firms in the payments market could give rise to a range of complex issues for the industry and policymakers in the period ahead.

Digital wallets such as Apple Pay, Google Pay and Samsung Pay are the most prominent examples of bigtech payment services that are rapidly gaining traction in Australia (see chapter on 'The Evolving Payments Landscape'). These digital wallets allow consumers to make contactless payments with a smartphone or other payments-enabled device, using near-field communication technology. In early 2021, the Bank made a submission to the Parliamentary Joint Committee on Corporations and Financial Services' inquiry into mobile payment and digital wallet financial services. The Bank's submission discussed the current state of the digital wallet market in Australia, the technologies that enable them and the business models adopted by different providers. It also outlined some of the potential policy issues arising from the increased use of digital wallets and the commercial arrangements of providers that are relevant to the Bank's mandate to promote competition, efficiency and safety in the payments system.

The Bank also welcomed the recent announcement that the Digital Finance Cooperative Research Centre (CRC) was selected to receive funding under the CRC Program administered by the Ministry of Industry, Science and Technology. The Bank is participating in the Digital Finance CRC as part of work on the Bank's strategic focus area of supporting the evolution of payments. Participation in the CRC will provide the Bank with an opportunity to collaborate with industry and academic partners on longer-term research related to innovations in digital finance, including asset tokenisation and CBDC.

Central bank digital currency

Many central banks, including the Reserve Bank, are researching the potential use, benefits and other implications of issuing CBDC as a complement to existing forms of money. A CBDC refers to a new digital form of money that would be issued by (and therefore be a direct liability of) a central bank, and could be used by households and businesses to make payments. Consideration of CBDC has generally distinguished between two broad use cases: a CBDC for retail (or general purpose) use, which would be like a digital version of cash that is essentially universally accessible; or a CBDC for wholesale use, which would be accessible only to a more limited range of wholesale market participants (such as banks and large corporates)

[4] Formerly the Senate Select Committee on Financial Technology and Regulatory Technology.

for use in wholesale payment and settlement systems.

The Bank has been researching CBDC for a number of years, exploring both retail and wholesale use cases. In September 2020, the Bank published an article that outlined some of the possible design considerations, and the case for and potential implications of issuing a retail CBDC.[5] The article highlighted a number of factors that indicated there was not a strong public policy case for issuing a CBDC for retail use in Australia at present. This included the fact that, even though the use of cash for transactions has been declining, cash is still widely available and accepted as a means of payment. There are also questions about whether there would be strong demand for a CBDC, given that Australian households and businesses are already well served by a modern, efficient and resilient payments system that has undergone significant innovation in recent years, including the introduction of the New Payments Platform (NPP). Despite not seeing a need to develop one at present, the Bank is continuing to monitor the case for a retail CBDC in Australia, including how it might be designed, the various policy implications and potential uses. Most recently, for example, the Bank has been engaging with participants in the payments industry on potential use cases for a retail CBDC that may not be adequately met through existing payment methods.

Separate to its work on retail CBDC, the Bank has been exploring the case for a wholesale form of CBDC. The Bank commenced technical experimentation on wholesale CBDC in 2018/19 with the development of a proof-of-concept (POC) of a tokenised form of CBDC using distributed ledger technology (DLT). The Bank extended this work in 2020/21 through a collaborative research project with the Commonwealth Bank, National Australia Bank, Perpetual and ConsenSys Software (a blockchain technology company). This project involved the development of a POC of a wholesale CBDC, but this time it explored how access to the CBDC could be extended beyond banks to a wider range of wholesale market participants. It also integrated a digital asset in the form of a tokenised syndicated loan to explore the implications of 'atomic' delivery-versus-payment settlement, as well as other potential benefits of combining CBDC and tokenised assets on interoperable DLT platforms. A report on the project will be published shortly.

The Bank is continuing to undertake research on CBDC as part of the strategic focus area on 'supporting the evolution of payments' in the Bank's Strategic Plan. This includes the establishment of a cross-disciplinary team focused on researching CBDC and the Bank's participation in the Digital Finance CRC. The Bank is also currently collaborating with the BIS Innovation Hub and a number of other central banks on 'Project Dunbar', which is exploring the governance and connectivity models that could support the use of multiple CBDCs for wholesale cross-border settlements.[6]

Regulation of stablecoins

The Bank has continued to monitor developments related to the emergence of so-called 'stablecoins', which are a type of crypto-asset designed to avoid the price volatility experienced by many other crypto-assets, such as Bitcoin. Stablecoins seek to maintain a stable value through various forms of asset backing or through the use of algorithmic techniques to try and match the supply of coins with demand, with the intention of making the stablecoin more attractive to hold as a store of value and as

[5] Richards T, C Thompson and C Dark (2020), 'Retail Central Bank Digital Currency: Design Considerations, Rationales and Implications', RBA *Bulletin*, September.

[6] See RBA (2021), 'BIS Innovation Hub and Central Banks of Australia, Malaysia, Singapore and South Africa Will Test CBDCs for International Settlements', Media Release No 2021-18, 2 September.

a medium of exchange. Stablecoins that become widely used in multiple countries could potentially make cross-border payments less expensive and overcome some of the challenges associated with financial exclusion. However, without appropriate oversight and regulation, stablecoins have the potential to be used for money laundering or illicit activities and could raise consumer protection and privacy concerns.

To date, most of the issuance of stablecoins globally has been concentrated in a small number of asset-backed arrangements that are pegged to the US dollar. There has been almost no issuance of Australian dollar-denominated stablecoins and their use as a payment method in Australia has been very limited. Even so, the Bank has been closely monitoring developments in this area. There are potential benefits for competition and innovation in the payments system from the development of stablecoins, and new arrangements could emerge that gain rapid adoption. It is therefore important for the Bank and other regulators to consider any policy issues that might arise.

A prominent overseas stablecoin initiative that has been seeking to launch is the Diem project (formerly called Libra), which is backed by a consortium of blockchain, payments and technology companies including a subsidiary of Facebook. When it was first announced in 2019, the intention was to issue a stablecoin for use in cross-border payments that would be fully backed by safe assets denominated in a basket of major currencies. The project was to have been governed and operated in Switzerland and was seeking a payment system licence from the Swiss Financial Market Supervisory Authority (FINMA). Bank staff participated in a global regulatory forum established by FINMA that shared information and views on the evolving Diem project.

The scope of the Diem project has changed significantly since the initial announcement, mostly in response to regulatory concerns. The latest change, announced earlier this year, involved a strategic shift in the project from Switzerland to the United States with a plan to issue only US-dollar stablecoins and to manage the associated asset reserves via a US-regulated bank. These changes would bring the project fully within the US regulatory perimeter and, as a result, the Diem Association has withdrawn its licence application with FINMA. While it is not known when Diem will launch in the United States, it is expected that a number of other companies, including a subsidiary of Facebook, will subsequently launch digital wallets (and eventually other services) through which customers will be able to access and use Diem stablecoins.

Recognising both the potential benefits and the risks related to stablecoins becoming widely used for payments, Bank staff have been participating in several regulatory groups focused on stablecoins. This includes a Financial Stability Board (FSB) working group that developed a set of recommendations published in October 2020 on the appropriate regulatory and oversight arrangements for global stablecoin arrangements. Domestically, the Bank is participating in a Council of Financial Regulators (CFR) working group established earlier this year to consider the domestic regulatory framework that should apply to private stablecoin arrangements. The working group, which also includes the Australian Transaction Reports and Analysis Centre, is currently working to assess how stablecoin arrangements would be treated under existing regulatory frameworks, with a view to identifying risks to consumers and the financial system and developing recommendations to address any regulatory gaps.

Regulation of stored-value facilities

The Bank has remained involved in work on the regulatory framework for stored-value facilities

(SVFs). These products encompass a wide range of facilities that enable customers to store funds electronically for the purpose of making payments. The Bank currently shares regulatory responsibilities for SVFs, also known as purchased payment facilities, with the Australian Prudential Regulation Authority (APRA) and the Australian Securities and Investments Commission (ASIC).

The CFR recognised the potential for SVFs to become a more prominent part of the Australian payments system and initiated a review of regulatory arrangements in mid 2018. The outcome of the review was a set of recommendations for a revised regulatory framework for SVFs aimed at modernising and simplifying regulation in a way that would be conducive to innovation, while providing appropriate consumer protections. The recommendations were delivered to the Australian Government in October 2019 and the government announced in October 2020 that it would implement the CFR's recommended reforms. Under the new framework, ASIC and APRA will continue to regulate individual providers of SVFs depending on the size and other characteristics of the facility. The Bank will no longer have a role in regulating individual SVF providers. Details of the new framework, which will require changes to legislation to implement, have not yet been finalised. Until the new framework is in place, the Bank, APRA and ASIC will continue to administer the current regulatory requirements for SVFs.

Regulation of electronic conveyancing platforms

Electronic conveyancing (e-conveyancing) refers to the digital completion of property conveyancing transactions. This includes the lodgement of property dealings with land registries, the exchange and disbursement of settlement funds, and the payment of associated duties and taxes. There are currently two e-conveyancing platform providers – Property Exchange Australia Ltd (PEXA) and Sympli Australia Pty Ltd – which operate in most states and territories. E-conveyancing offers a number of benefits over traditional paper-based arrangements, including improved efficiency and reduced costs. Recognising these benefits, a number of states and territories have mandated the use of e-conveyancing for all or most real property transactions.

The regulatory framework for e-conveyancing is administered by the Australian Registrars' National Electronic Conveyancing Council (ARNECC), which comprises the state and territory Registrars. While the Bank does not have a supervisory mandate in relation to e-conveyancing, it chaired a CFR working group that was established in March 2020 with representatives from the ACCC and ARNECC to review elements of the regulatory framework for e-conveyancing. The purpose was to identify whether enhancements to the regulatory framework in relation to payments and financial settlement aspects of e-conveyancing could promote consumer protection, resilience and competition in the e-conveyancing market.

At its June 2021 meeting, the CFR and ACCC supported the recommendation of the working group to strengthen the regulatory arrangements for e-conveyancing through the development of a self-regulatory regime. It has been agreed that an industry code will be jointly developed by the e-conveyancing platform providers and financial institutions under the governance of an industry steering committee facilitated by Australian Payments Network (AusPayNet). Development of the code is expected to be completed by September 2022, subject to any necessary authorisations by the ACCC.

Promoting operational resilience in retail payments

With the growth in electronic payments and the reduced use of cash, the operational resilience in the electronic retail payment system is attracting greater focus. Major disruptions or data breaches in these systems could have a material negative impact on end users and economic activity, and significantly reduce public confidence in payment services and key providers. At the same time, operational challenges facing providers of retail payments are rising in association with greater complexity in payments infrastructure and services, and growing cyber threats.

Data collected from banks and other financial institutions show a substantial rise in the number and total duration of operational outages to retail payment services in recent years. The Board considers it vital that entities in the retail payments industry invest in resilient systems and maintain reliable services to customers. Accordingly, the Bank has been working with retail payments providers on an initiative to improve the quality and transparency of information about the reliability of their services. This initiative involves enhancing the Bank's existing data collection for retail payments incidents, and developing a set of quarterly operational reliability statistics for retail payment services that individual providers will publicly disclose on their websites. The new quarterly data collection has recently commenced, and the Bank expects the first public disclosures on service availability and significant outages to be made by institutions in November. Better and more transparent information about the reliability of retail payment services is intended to raise the profile of this issue among financial institutions and their customers, and to enable improved benchmarking of operational performance. The Board will monitor the reliability of retail payment services using the new data and will consider whether any further policy measures are needed to enhance operational resilience.

The Bank has also been assisting the Department of Home Affairs to apply the government's reforms to critical infrastructure legislation to the retail payments system. In April, the Department released a consultation paper specifying several real-time retail payment systems as critical from a security and reliability perspective: the Mastercard debit and credit card systems; the Visa debit and credit card systems; the eftpos card system; and the NPP.[7] The intention is that the entities responsible for the operation of central infrastructure assets in these systems will be subject to obligations with respect to their management of cyber risks and other hazards (such as the maintenance of a risk management program and incident reporting). Providers of payment services that are authorised deposit-taking institutions (ADIs) will not be captured in the reforms for the payments sector, since they are regulated by APRA and subject to its existing prudential standards.

Payments security initiatives

Payments security is an increasingly important feature of the retail payments system given the ongoing rise in online and other electronic payments. Payments-related fraud imposes significant costs on consumers, businesses and financial institutions, and can undermine public confidence in electronic payments. The Board has for many years been monitoring developments in retail payment fraud and supporting industry initiatives to bolster payments security.

A major focus for the payments industry in recent years has been on implementing measures to address rising fraud related to card-not-present (CNP) transactions (i.e. online,

[7] See Department of Home Affairs (2021), 'Protecting Critical Infrastructure and Systems of National Significance: Draft Critical Infrastructure Asset Definition Rules', April. Available at <https://www.homeaffairs.gov.au/reports-and-pubs/files/critical-infrastructure-asset-definition-rules-paper.pdf>.

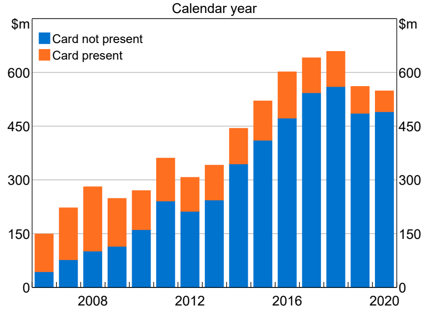
phone and mail-order card purchases). These measures include standards aimed at safeguarding the card data held by merchants, the increased tokenisation of card details and improved fraud detection systems. The industry, led by AusPayNet, also introduced the CNP Fraud Mitigation Framework, which came into effect in July 2019. This framework requires card issuers and merchants to put in place 'strong customer authentication' (multi-factor authentication) for online transactions if specified fraud thresholds are consistently breached.[8] These various measures have contributed to a recent modest decline in CNP fraud losses, following the upward trend seen over the past decade or so (Graph 3.1).

While losses from unauthorised use of cards have fallen recently, losses associated with customer data theft and scams have become more significant. Payment scams occur when people are deceived or manipulated into sending funds or personal information to criminals – for example, when scammers offer an attractive investment scheme that is fake, or send a fake bill from a legitimate business seeking payment. According to data published by the ACCC, financial losses from scams have grown substantially in recent years (despite the fact that many scams go unreported by victims). In 2020, there was an increase in scam activity associated with the pandemic as people were interacting more with businesses and governments online, creating more opportunities for scammers.

Graph 3.1

Card Payment Fraud Losses*

Calendar year



* Includes card fraud losses for international card schemes, Visa and Mastercard, and the domestic card scheme, eftpos, that are issued and/or acquired in Australia

Source: AusPayNet

To help combat growing payment scam losses, banks have been investing more in measures to detect and respond to scam activity, as well as to educate their customers on the risks and the precautions they can take. The industry is also working to better understand scam activity by improving the classification and reporting of scam data, and by sharing information about scams. Further industry efforts to raise awareness of scam risks and to strengthen fraud detection and prevention will be important as account-to-account transactions grow. The Board notes that the wider use of the NPP PayID addressing system – which allows the payer to check that the payee name matches their expectation – is one possible way to help reduce the incidence of certain types of scam payments.

Another development that could help prevent fraud and scams is the rollout and adoption of digital identity services. These are services that enable individuals to establish a digital identity to prove who they are when interacting online with businesses and government, which can significantly improve the security and convenience of online transactions. The payments industry is continuing to work on developing governance arrangements for the TrustID digital identity framework, which was developed by the Australian Payments Council (APC) in 2019 to facilitate the emergence of a network of interoperable digital identity services. There has been some progress over the past few years, with digital identity services such as

[8] 'Strong customer authentication' involves verifying that the person making the transaction is the actual cardholder using two or more independent authentication factors drawn from: something that only the customer should possess (e.g. a card or mobile device); something that only they should know (e.g. a PIN or password); and something the customer is (e.g. a biometric feature such as a fingerprint or facial profile).

Australia Post's Digital iD and eftpos' ConnectID having launched, and other pilots underway. However, the number and reach of services remains relatively limited at present. The Board has been disappointed by the slow rollout of private-sector digital ID services in Australia given the rapid shift to online transactions associated with the COVID-19 pandemic and the fact that other jurisdictions have made significantly more progress in making these services available.

There has been more success with the rollout of digital ID in the government sector, with the myGovID service now being used by over 4 million Australians and 1.2 million Australian businesses to securely and conveniently access 80 government online services. The Digital Transformation Agency has recently been consulting on planned legislation aimed at expanding the Australian Government's digital ID system into a whole-of-economy solution, offering access to state, territory, local government and private sector services, and allowing entities in other digital ID systems to apply for accreditation under the Trusted Digital Identity Framework. Improved interoperability between the private- and public-sector digital ID schemes should support the increased adoption and use of digital ID services in Australia.

Enhancing cross-border retail payments

Having access to efficient, competitive and safe cross-border payment services in Australia is becoming more important as households and businesses increasingly look to send or receive payments across borders. Yet bank-intermediated cross-border payments have typically been far more expensive, slower and more opaque than domestic payments, even considering the additional risks and complexities involved in processing these payments. These challenges are most evident for low-value international money transfers – in part, because of longstanding frictions in the correspondent banking arrangements used to process these transfers – although users of most types of cross-border payment services face at least some of the challenges.

Accordingly, enhancing the efficiency of cross-border retail payments remains a priority for the Bank's payments policy work. Bank staff are contributing to a number of international working groups that are implementing aspects of the G20 Roadmap for Enhancing Cross-border Payments (see Box A). The Bank has also been engaging with domestic industry stakeholders about Australia's contribution to the Roadmap work.

The Bank continues also to monitor competition and access issues associated with the entry of new technology-enabled providers of cross-border retail payment services into the Australian market. Gains in market share for these providers over recent years has been a factor spurring incumbents to lower prices and improve the convenience of their offerings. However, many non-bank providers have found it difficult to obtain or retain reasonable access to the core domestic banking services and payment infrastructures that they need to provide cross-border payment services to Australian customers.

The Bank is concerned that this type of 'de-banking' could impede competition and innovation in the market for cross-border retail payment services (as well as other types of financial services where fintechs and other non-bank providers have been de-banked). Accordingly, the Bank is working with other Australian regulatory agencies to explore the underlying causes and possible policy responses to de-banking. The Final Report of the Treasury Payments System Review has recommended the introduction of a single tailored licensing framework for (non-bank) payment service providers, to facilitate access by these entities to payment systems and possibly help alleviate de-banking risks.

Improving the cost and accessibility of low-value transfers (or remittances) to the South Pacific countries is another important focus of the Bank's cross-border payments work. Given the relatively small size of these remittance flows, it has tended to be more costly to transfer funds to South Pacific countries than other countries, and non-bank providers servicing these corridors from Australia have faced significant de-banking risks. This is a particular problem because many people in South Pacific countries rely heavily on remittances from family and friends in Australia (as well as New Zealand). The Bank (together with the Reserve Bank of New Zealand, other South Pacific central banks and multilateral organisations) is working on a possible regional Know-Your-Customer (KYC) utility that may help support the flow, and potentially also reduce the cost, of remittances to the South Pacific. This initiative involves consulting with commercial banks, money transfer operators and other key stakeholders in the remittance sector. The facility would have inbuilt KYC compliance workflows that ensure entities using the facility can perform KYC compliance checks to a high standard, and can demonstrate this to banks and regulators. If feasible, it is expected the facility would take several years to build and implement.

Migration to ISO 20022 messaging standard

The Board is monitoring the progress of a major industry-led program to update the messages used in the Australian High Value Clearing System (HVCS) to a new format based on the ISO 20022 standard. The HVCS is used by financial institutions to clear high-value customer payments, correspondent banking flows and the Australian dollar leg of foreign exchange transactions, with settlement occurring in the Reserve Bank Information and Transfer System (RITS). Currently, HVCS payments, like other payments processed over the Society for Worldwide Interbank Financial Telecommunication (SWIFT) network, use a proprietary message format. SWIFT plans to migrate cross-border payments sent across its network to the ISO 20022 format, commencing in November 2022, with a goal to eventually migrate all cross-border payments and reporting traffic to the new format by November 2025. A number of jurisdictions have already adopted, or are working towards adopting, ISO 20022 for domestic payments ahead of SWIFT's cross-border payments migration deadline.

In 2019, the Bank undertook a consultation on the migration of key parts of the payments system on behalf of the Board and the APC. The payments industry has now completed the design and planning of the HVCS migration, and the program is currently in the build stage. A co-existence phase – where both ISO 20022 and the existing message formats will be supported for certain payment types – will begin in November 2022. During this phase, ISO 20022 messages with enhanced data content must be used for domestic payments relating to correspondent banking and cross-border flows where the original payment instruction is in the ISO 20022 format, but other HVCS transactions can continue to use the existing message formats. Full transition to ISO 20022 is planned for completion by November 2024.

The adoption of ISO 20022 for the HVCS is expected to provide a number of benefits. ISO 20022 messages are able to carry enhanced data content, which can assist financial institutions in meeting their financial crimes obligations and combatting payments fraud, as well as supporting innovation. The standard also offers a range of potential processing efficiency enhancements, such as improved straight-through processing, and has been designed to adapt to new requirements and technologies as they emerge. As the NPP already uses ISO 20022, adopting the standard for the HVCS is one step towards potentially enabling messages to be redirected between the two systems in a contingency, which would enhance the resilience of the payments system. The global adoption of ISO 20022 is one of the initiatives in the G20 Roadmap for Enhancing Cross-border Payments (see Box A).

New Payments Platform

The Board continues to have a close interest in the adoption of the real-time payments capability of the NPP and especially the development of new functionality to meet the evolving needs of end users. For the past few years, NPP Australia (NPPA) has been publishing semi-annual updates to its capability development roadmap with its schedule of plans to extend and enhance the platform's native capabilities. One element of the roadmap implemented earlier this year was the introduction of new data-rich message standards for superannuation, tax, payroll and e-invoicing payments. These standards define the specific data elements that should be carried with these payment messages, which will allow for more business automation, improved reconciliation and straight-through processing of these types of payments. From April, all NPP participants were required to be able to receive these messages, and it is expected that institutions will compete to develop capabilities that allow their customers to send these types of payments through the NPP. The adoption of these message standards should also support the industry in migrating bulk payments such as payroll, which are currently made through the Direct Entry system, to the NPP.

A key element on the current NPP roadmap is the development of the 'PayTo' service, which will enable customers to authorise third parties to initiate payments from their bank accounts using the NPP. This service will provide an alternative to direct debits where customers will have greater transparency and control over their payment arrangements, and will also support the use of bank accounts for in-app and other types of recurring payments. The PayTo service could also be one of the ways in which financial institutions meet any potential obligations to deliver payment initiation under the Consumer Data Right. Implementation of the PayTo service is a significant project for the industry. Notwithstanding some recent delays associated with the degree of internal work required by participants and the impact of COVID-19, the service is scheduled to launch in mid 2022.

By the end of 2022, all NPP participants will also be required to join the NPP international payments business service, which will allow banks and other international payment service providers to use the NPP for the final leg of international payments coming into Australia. This business service will use the data richness of NPP payment messages to incorporate additional data elements that will allow a receiving bank to perform the necessary due diligence and financial crimes screening of payments to meet its regulatory obligations. The adoption of this service by NPP participants will support safer and faster cross-border payments.

Besides encouraging the development of new NPP functionality, the Board has also been monitoring access to the NPP, with a focus on ensuring that there are competitive and safe access options for payment service providers wishing to utilise the NPP. As of the end of August 2021, there were 106 entities using the NPP to provide payment services to their customers; this includes 93 entities (eight of which are non-ADIs) that are indirectly connected to the NPP via one of the direct participants. The Bank made a number of recommendations on NPP access as part of a joint consultation with the ACCC in 2019. A follow-up review of NPP access and functionality was planned to commence this year, but was postponed while the ACCC considered NPPA's merger with BPAY and eftpos, and also pending the outcome of the Treasury Review of the

Payments System. The Bank is currently expecting to commence this review in 2021/22.

Policy issues associated with declining cash use and the supply of cash services

There has been a structural decline in the use of cash for transactions in Australia as consumers increasingly prefer to use electronic payment methods (such as cards), with the COVID-19 pandemic contributing to a further step down in cash use. This trend has been seen in a significant decline in cash withdrawals; although, the value of banknotes in circulation has continued to increase in recent years, reflecting ongoing demand for cash for precautionary and store-of-wealth purposes.

The Board has been monitoring these trends in cash use closely and is keen to ensure that any associated changes in the availability or acceptance of cash do not cause undue hardship for people. The decline in the transactional use of cash is impacting the economics of providing cash services, which could prompt providers to reduce the supply of cash services. This could become a policy concern given that cash is still heavily used by some segments of the population; cash also serves as an important backup payment option during outages in electronic payment services. Given these issues, the Bank has committed to working with the payments industry to support the ongoing provision of cash services.

There has been a significant reduction in the number of cash access points in recent years, with the number of bank branches continuing to fall and a decline of around 20 per cent (6,500 machines) in the number of active ATMs since its peak in late 2016. However, research by Bank staff published in June 2021 found that the majority of Australians continue to have good access to cash deposit and withdrawal services through bank branches, ATMs and Australia Post 'Bank@Post' services.[9] Regional and remote areas, however, have poorer access with fewer alternative cash access points, making these areas more vulnerable to any further removal of services. The continued presence of Bank@Post services is increasingly important in many regional and remote areas.

The Bank has also conducted surveys to investigate cash acceptance by retail merchants. The last survey, conducted in September 2020, found that the vast majority of businesses continued to accept cash as a means of payment, although the share accepting cash had declined marginally since the onset of the COVID-19 pandemic.[10] However, as cash use declines further, it is possible that more merchants may decide to stop accepting cash, for example, if they judge that the benefits of not accepting cash (e.g. in lower cash handling costs and faster checkout times) outweigh the costs (e.g. from lost sales from cash-only customers or during outages to electronic payments). Bank staff are currently participating in an APC working group that is examining trends and drivers of cash acceptance among merchants with a view to informing any policy concerns that might arise.

The Bank has also been engaging with banks and cash-in-transit operators on the challenges of supplying cash distribution services as cash use declines. These discussions have highlighted a range of actions that have been taken, or could be considered, to improve efficiency and reduce the costs of providing cash services. Several banks have recently sold parts (or all) of their off-branch ATM fleets to third-party operators, which are looking to operate these ATM fleets on a utility basis where banks can pay for their customers to access the machines fee free. In an environment of declining ATM use and where the costs of ATM deployment have been rising, such arrangements could be a more

[9] See Caddy J and Z Zhang (2021), 'How Far Do Australians Need to Travel to Access Cash?', RBA *Bulletin*, June.

[10] See Guttmann R, C Pavlik, B Ung and G Wang (2021), 'Cash Demand during COVID-19', RBA *Bulletin*, March.

efficient way to sustain a broad coverage of ATMs, which may be particularly important for regional and remote areas that often have fewer options for accessing cash services.

The pressures posed by the trend decline in cash use are also having implications for the economics of wholesale banknote distribution, which is the process by which banknotes are obtained from the Reserve Bank by financial institutions and moved around the country via cash-in-transit companies. This system is critical to facilitating the flow of cash in the Australian economy. The Bank has announced it will shortly be commencing a consultation on banknote distribution arrangements to investigate if any policy action is warranted.

More broadly, the Board will continue to monitor access to cash services and trends in the use and acceptance of cash, including through the Bank's regular Consumer Payment Surveys. The Board will also consider whether any policy actions by the Bank might be required to support the continued provision of cash services during the transition away from cash.

The future of the cheques system

The use of cheques in Australia has continued to decline at a rapid rate in recent years, and the COVID-19 pandemic is likely to have accelerated this trend as more people adopt digital alternatives. The total number of cheque payments declined by 25 per cent in 2020/21, compared to an average annual rate of decline of 20 per cent over the previous five years. There were less than 1.5 cheque transactions per person in 2020/21 and cheque payments accounted for less than 0.3 per cent of all non-cash payments. The rapid decline in the value of cheques in recent years has been driven by a sharp fall in the use of financial institution (bank) cheques for property settlements associated with the increased adoption of e-conveyancing platforms; personal and business cheque use has also been declining as more payers transition to electronic payment methods.

As cheque use continues to decline, the per-transaction cost of supporting cheque payments, which is already high relative to other payment methods, will continue to rise. From an efficiency perspective, there will be benefits in winding up the cheque system at some point given the high cost of maintaining it and the increased availability of payment methods that can meet similar payment needs. However, it is also important that the payment needs of different users are identified and addressed to ensure that no one is left behind.

The Board has been monitoring the industry's efforts in managing this transition, including the strategy currently being overseen by AusPayNet to support a customer-led migration away from cheques. The strategy has various elements, including: helping to identify and communicate viable payment alternatives to remaining cheque users through community outreach and education; reviewing the Australian Paper Clearing System rules to ensure they provide a path for financial institutions to withdraw from providing cheque services if they wish; and advocating for payments neutrality in any government legislation and regulations that currently require or promote cheque use. Financial institutions also have an important role to play in assisting their customers to transition to viable alternative payment methods and giving reasonable notice of any plans they may have to transition away from providing cheque services.

The Board has been broadly comfortable with the approach the industry has been taking on this issue, and the Bank will continue to engage with the industry on the orderly wind-down of the cheques system in a way that enables the payment needs of remaining cheque users to be adequately met.