



NATIONAL AUSTRALIA BANK

**RESPONSE TO RBA ON POTENTIAL DESIGNATION OF
EFTPOS & ATMs**

July 2004

1. Introduction

The National fully supports the reform of EFTPOS debit card and ATM interchange and has been an active participant in both industry working groups formed at the behest of the Reserve Bank of Australia (RBA). We believe that the objective of this reform should be to achieve a simpler, more efficient and transparent pricing regime for both EFTPOS and ATMs.

In general, we would prefer a collaborative voluntary approach to reform, as opposed to designation. However we acknowledge that the voluntary reform approach to date, particularly for EFTPOS, has not achieved a satisfactory outcome. This submission sets out the National's views for both EFTPOS and ATM interchange and access reform.

The National reserves its position in relation to making further submissions on various matters raised in this submission, and in general, in relation to the overall progress of the RBA's program of regulation and reform for EFTPOS and ATMs.

2. Views on EFTPOS Designation

Overview

The National is still of the view, (as stated in our submission of September 2002 to the RBA on Debit Interchange Reform) that the most logical approach to determine interchange for EFTPOS debit cards is to apply the same economic principles that were used by the RBA for Credit Card reform.

If this were so, issuer costs such as transaction processing, authorisation, fraud and fraud prevention would be the only "eligible" costs used to calculate the interchange fee, and would result in a small interchange fee of about \$0.07 per transaction payable by the acquirer to the issuer¹.

We also stated in our September 2002 submission that we supported the move to zero interchange on pragmatic grounds, taking into account the desire of regulators and stakeholders to achieve simultaneous debit and credit reform. Clearly simultaneous interchange reform did not occur.

We would understand why the RBA might designate and rapidly put in place a zero interchange standard to bring about finality to the process. If the RBA does not move rapidly to bring finality in this way, we would favour a small positive interchange.

Public Benefits of EFTPOS interchange reform

The move to multilateral EFTPOS interchange either zero or a small amount paid by the acquirer to the issuer would result in a number of benefits to the public:

- EFTPOS would become more attractive to consumers, as competitive forces are likely to reduce cardholder fees over time, thereby inducing a shift towards the use of EFTPOS and reducing the overall cost of the Australian payments system.

¹ Debit and Credit Card Schemes in Australia, A Study of Interchange Fees and Access - Reserve Bank of Australia, Australian Competition and Consumer Commission - October 2000

- Entry as a new issuer or acquirer of EFTPOS transactions would become easier by simplifying the negotiation of bilateral interchange agreements.

Access

The National favours continuing to allow the current voluntary reform process for access being run by APCA instead of any potential designation of the EFTPOS system.

APCA has set up the EFTPOS access project with the intention to establish rules as to the entitlements and attendant obligations of parties seeking to participate in the exchange of EFTPOS transaction data in relation to:

- Establish physical connections to exchanging and/or switch EFTPOS transaction data.
- Provide clearing and settlement services for EFTPOS transactions.

APCA intends that the EFTPOS access regime being developed will provide:

- Standardised commercial terms and conditions under which parties that wish to exchange EFTPOS transactions data deal with one another.
- Standardised process for the set up of new physical connections between parties that wish to exchange EFTPOS transaction data.
- Some form of regulation of the changes to be paid for establishing physical connections between parties that wish to exchange EFTPOS transaction data.
- Dispute resolution processes for dispute between parties that wish to exchange EFTPOS transaction data in relation to the provision of physical connection and also in relation to the provision of clearing and settlement services.

Our reasons for supporting the voluntary reform being run by APCA are:

- APCA has developed a comprehensive project plan with clear and distinct milestones and is currently on schedule.
- APCA and its Board are committed to develop a practicable and equitable access rules as is demonstrated by the level of expenditure and resource (both internal and external) being expended on the project.
- APCA has established a working group not only consisting of its members but other stakeholders such as First Data International, the Australian Retailers Association, Woolworths, the Australian Institute of Petroleum and the RBA.

3. Views on ATM Designation

Overview

As a general approach, the National favours voluntary reform, however, as with EFTPOS we understand why the RBA would seek to designate for ATMs.

If the RBA was to designate, the National favours in principle, the implementation of the direct charging model, that has been developed by the ATM Industry Steering Group (AISG) over the last two years.

The model, as developed by the AISG, is designed to generate enhanced competition, more transparent fee disclosure and encourage a wider ATM network. The introduction of this model is likely to result in a more market driven pricing regime with fees for the use of Foreign ATMs being more closely aligned with costs.

Model Overview

The key features of the proposed model are:

- No interchange fees are charged between parties covered by the model (ie current interchange fees are reduced to zero). This would be replaced with the ability for direct charging of the cardholder for the use of foreign ATMs by the ATM operator and Card issuer.
- Disclosure of the existence and amount of any direct charge to the Cardholder prior to the Cardholder committing to the foreign ATM transaction by the ATM Operator.
- Ability for the Cardholder to cancel the foreign ATM transaction without charge.
- Debiting of the ATM Operator Fee to the Cardholder's account in conjunction with a balance inquiry and/or cash withdrawal or other ATM transaction for which an ATM Operator Direct Fee may be charged.
- Settlement between the Card Issuer and the ATM Operator (or the ATM Acquirer) of both amounts (cash withdrawal and direct charge).
- Disclosure of the possible existence (but not necessarily the amount) of a Card Issuer Transaction Fee prior to the Cardholder committing to the foreign ATM transaction.
- Separate charging of the Card Issuer Transaction Fee (if any) from any ATM Operator's Direct Fee charged to the Cardholder.
- Allowing market forces to determine the level of fees charged by the ATM Operators and Card Issuers.

Taking into account the distribution difficulties of smaller financial institutions due to smaller ATM fleet sizes we can appreciate the impact a pure direct charging model would have on them. On that basis, we support the establishment of a direct charging model, as developed by the AISG, that supports the positive competitive and public benefits provided by small aggregate networks, without diminishing the benefits of direct charging.

However, while the National is in broad agreement with this model we believe that some fine tuning and clearer definition is required. In particular, how members of the aggregate networks that operate outside the direct charge environment are treated needs to be clearly defined, as well as the level volume increase required for those network members to potentially move to a direct charging environment.

Also consideration needs to be given as to the implications on direct charging should one of the smaller financial institutions decide to change networks.

Public Benefits

The National believes that the proposed direct charging model is in the public's interest. It will create a more dynamic, competitive environment by moving from an

arrangement where prices are composite, insufficiently transparent and relatively inflexible, to an arrangement where prices will be abundantly more transparent to the consumer and significantly exposed to competitive market forces.

In addition the model will:

- Create economic incentives for an expanded ATM network.
- Provide enhanced consumer choice and convenience.
- Result in the unbundling of existing foreign ATM fees.
- Provide transparent fee disclosure at the point of the foreign ATM transaction.
- Increase competition between ATM Operators, ATM Acquirers and Card Issuers
- Help to align transaction prices more closely with costs.

In terms of the National Australia Bank's fee policy for access to services such as ATMs we affirm our commitment that we will not price differentiate between urban, country and rural areas.

Access

The National recognises the importance of the issue of access to the ATM network as a means of improving competition. The National favours allowing APCA to develop access rules along the same lines as it is already doing for EFTPOS.

As part of its operation, the AISG asked APCA to undertake a project to develop conditions of entry, which would facilitate access to the ATM network in the context of Direct Charging for Foreign ATM Transactions. We would support the continuation of this work.