Mr Christos Fragias

28 January 2020

Head of Payments Policy Department

Reserve Bank of Australia

GPO Box 3947

Sydney NSW 2001

Delivered via email to: pysubmissions@rba.gov.au

RE: Feedback – Review of Retail Payments Regulation: Issues Paper (November 2019)

To Whom It May Concern:

Thank you for the opportunity to provide feedback regarding the subject under reference. Retail payments in Australia has undergone significant innovation, structural and regulatory changes in recent years.

Largely reflecting the development in global payments technologies, along with ongoing regulatory developments, with both significantly contributing to, and shaping the retail payments landscape in Australia.

In light of this, please find below, in the following pages, my feedback to selectively targeted questions raised by the Reserve Bank of Australia (the Bank), in its Review of Retail Payments Regulation: Issues Paper (November 2019).

Please ensure to supress or black out my residential address and signature provided in this cover letter. I am satisfied only for my name to be published.

Finally, I would welcome the opportunity to discuss my responses in greater detail directly with the Bank.

Yours Sincerely,

Christos Fragias

Q1: What major recent or prospective developments in the broader payments industry are particularly relevant to this review? More specifically, are there any gaps in functionality available to end users or any shortcomings in industry governance or operating arrangements that require regulation or coordinated industry action?

In reference to the points raised in the above question specifically on:

- Gaps in functionality available to end users;
- Industry governance; and
- Coordinated industry action.

Australia does appear to lag behind other countries in the provision and timing of the development and implementation of retail payments technologies, including the New Payments Platform (NPP).

For example, if we look at the UK, when it introduced Faster Payments approximately a decade prior to Australia's NPP, it did so without the delays from multiple implementation dates pushed back, that Australia has experienced.

Equally, UK consumers did not encounter limited service provision from their banks, to the procrastinated degree which Australian customers have, as domestic banks continue to build full NPP capability. Recognising the number of years domestic banks had leading up to the planning, building, developing, and testing and implementation of their fast payments solutions, and adding now the two years after the NPP's implementation, with full service capability yet to be achieved.

These delays have resulted in a source of customer frustration, that their banking institution has not met their expectations, in fulfilling their wholistic fast payments needs and experience[1].

Additionally, the media has reported more than one incident of data breach to NPP participants' customer stored PayID[2]. These incidents have not contributed to strengthening customers' perception on the integrity and resilience of the NPP utility.

The Bank would benefit in mirroring similar regulatory approaches applied by the UK's Financial Conduct Authority (FCA), where in the past, the FCA has applied **enforceable undertakings** or other **regulatory directives** on UK banks, to meet their obligations in the timed rollout of market changes impacting banking services.

Q2: Are there aspects of retail payments regulation that lead to market distortions or that create opportunities for regulatory arbitrage? If so, what options should be considered as a means of addressing these? Are there gaps in the regulatory regime that need to be addressed or any elements where regulation is no longer required?

No feedback is provided at this stage.

Q3: Are there barriers to innovation and/or competition that may affect the costs of or provision of electronic payments and should be addressed in this review?

No feedback is provided at this stage.

---

[1] References to customer and cardholder in this feedback document, can be interchangeably used by the reader.
[2] *"PayID breach sees customers' banking information hacked"* - news.com.au, 25 August 2019, Reid, I.

Q4: How do stakeholders assess the functioning to date of least-cost routing (LCR) of contactless debit card payments? Do additional steps need to be taken regarding LCR to enhance competition and efficiency in the debit card market?

Since the introduction of contactless transactions in Australia, the cost of accepting these card transaction types remains higher in interchange than opposed to a merchant accepting other card transaction types.

For example, Mastercard Australia's website notes the interchange category name, ***Tokenised Contactless*** is set at 0.88 per cent for Australia intra-country credit POS interchange, including GST. Set equal highest with Mastercard's *Commercial Executive* interchange category name for Australia intra-country credit POS interchange, including GST. And higher than the interchange category name, *Consumer Elite and Super Premium,* where interchange is set at 0.858 per cent, including GST.

Equally, for debit cards, where purchases exceed AUD $15, Mastercard's Australia intra-country debit POS interchange category name, ***Tokenised Contactless – Other (> AUD 15)*** is ranked equal highest at AUD $0.165 with two other debit interchange category names *(Other Card **Present** – **Premium**, and Other Card **Not Present** – **Standard**)*[3].

It is interesting how Mastercard has equally priced these last two interchange categories at the same interchange fee, despite one being **card present**, and the other being **card not present**[4]. The latter of which (i.e. card not present), has been reported to incur a higher risk of card fraud.

Further, ***standard*** interchange rates are usually applied by card schemes as a fallback *(i.e. to a higher or even highest rate of interchange)*, when a scheme participant fails to qualify for the interchange rate fee applied for when they submit transactions via a scheme's network for processing and settlement, and as a result, incurs the higher (fallback) *standard* interchange fee instead. While tokenization is a very secure protocol to accept card payments, though again, incurring the same interchange rate fee as the abovementioned card not present and *standard* interchange category names.

Ironically, contactless transactions, especially those where a customer is not required to enter their PIN at the terminal, as the transaction value resides under a pre-specified limit, are deemed low value transactions. And, if interchange was established, among other reasons, to fund fraud reduction strategies, there is a case as to why interchange for low value contactless transactions are set at levels mentioned above, equal to *standard*, when the risk factor for contactless payments compared to credit card fraud, especially card not present credit card fraud, appears lower.

There has been some debate within the industry that the unintended consequences of contactless technology have cannibalized issuers' credit card interchange revenues which potentially has seen higher contactless interchange rates to compensate, as more customers transition to, and increase their use of contactless, especially contactless debit, in favour of credit cards.

One challenge that has impeded in the rollout of LCR has been a lack of a timely and coordinated effort by industry participants. With the Bank, at times, and commendably, gaining further inroads by seeking **commitments** from institutions to have enabled LCR capability in the market, this indicates the industry needs more coercion, when the preferred outcome would see the industry achieving heightened proactive participation.

---

[3] It is noted on Mastercard Australia's website, a few interchange categories for debit incur an **ad valorem** rate.
[4] Mastercard Australia - Understanding Interchange.

While smaller and agile acquirers have launched LCR capability, the four majors, whom all enjoy prominent market share in several other banking and financial products and services, are taking longer than expected to have this functionality fully deployed to their merchants. This has been a source of frustration expressed across the regulatory and industry spheres.

Further exacerbation has been reported by the industry body, the Australian Retailers Association (ARA), that the ANZ mandates their merchants to display signage disclosing to customers that all dual network debit card transactions are routed via the ePAL network, where the ARA has called out that the Bank does not deem this to be a requirement placed on merchants[5].

Most recently, in a financial article, the ARA advised it was forming an industry alliance with other industry retail bodies to make a submission to the Bank regarding industry's lack of capability for LCR transactions[6]. In this same article, it was reported by the ARA's executive director that:

> *"Some banks won't give merchants Low Cost Routing because they're claiming to be giving them a better rate on debit and credit cards because they bundle them together,"*

While regulatory actions could be considered in further expanding the use of LCR, ultimately, merchant and customer education will raise awareness of payment options provided to each of these two parties. This will better inform merchants to participate in LCR transaction acceptance, and for customers to decide whether they wish to have their transactions routed to a lower cost scheme, or otherwise.

Q5: Have recent and prospective developments in technology changed the case for promoting the continued issuance of dual-network debit cards? What policy actions might be needed to promote competition and efficiency in an environment where single-network cards were more prominent? Alternatively, would it be desirable to mandate (or incentivise through interchange caps) that all debit cards issued enable at least two unaffiliated/competing networks?

Recently, the financial press reported that some customers have been charged excessive fees for the use of their dual-network debit cards (DNDC). Some major retailers in Australia have recently reconfigured their card payment acceptance systems to route international scheme debit transactions via the ePAL network. However, owing to these specific debit cards carrying a monthly threshold on the number of ePAL transactions permitted free of charge, breaching this monthly threshold has resulted in fees being charged to cardholders, and have taken cardholders by their unpleasant surprise[7].

In one example, a cardholder claimed they were charged AUD $18, and owing to public outcry, a spokesperson from Coles, recently advised the media:

> *"a small number of financial institutions have elected to charge their customers high fees for paying with Eftpos at any retailer in Australia".*

---

[5] *Least cost routing goes lives amongst ARA criticism* - East & Partners. 4 April 2019.
[6] *Retailers unite to fight for lower 'tap and go' card fees.* The Australian Financial Review. 28 January 2020., Mitchell., S.
[7] *The new hidden fee most Coles customers don't know about - have you been stung?* Yahoo News. 16 January 2020., Rolfe., B.

Despite a separate media statement by an ePAL spokesperson advising that cardholders should not be impacted by these charges, this leaves little hope that ePAL's comments will prompt affected issuers to take immediate action and remediate. Recognising that it could be argued that these cardholder charges are a negative by-product arising for the benefit of the merchant to lower their card acceptance costs, while simultaneously resulting in a customer's increase in their card usage fees.

While the Bank may look at mandating regulation to all debit cards issued are compatible to be routed to at least two competing scheme networks, the lack of Australia's underlying payments infrastructure not being fully LCR capable yet, further exacerbates this matter.

Therefore, we can acknowledge several factors needed to ensure LCR and DNDC capability works properly to promote an efficient payments system. These include:

1. DNDC functionality across issuers and schemes;
2. Infrastructure developed and capable of facilitating LCR for DNDCs;
3. Merchant education and awareness;
4. Customer education and awareness;
5. Regulatory measures to promote and oversee these payments capabilities; and
6. Representation by industry representative bodies.

The Bank should be just as, if not already, more cognisant that **customer usage is what will drive this initiative**. As more customers become informed of these fees levied upon them unexpectedly, as is the case here, their mitigation against more fees under the circumstances, is to insert their card at the terminal and select 'credit', as reported by the media. Which only slows down the transaction and moves against the spirit of why contactless payment technologies were introduced.

However, as customers better understand the benefits of LCR, driven by industry and regulatory awareness initiatives, customers may pressure their banks to accelerate the procrastinated rollout of LCR across merchants.

Therefore, the Bank should avert customer fee increases when considering the implementation of new payments regulation, to ensure not only merchants benefit from lower card acceptance costs in this case, however, customers also benefit from no excess fees, and a seamless payments experience. Thereby, motivating and benefiting cardholders to contribute in driving the Bank's regulatory objectives.

Ultimately, if cardholders are not seeing nor experiencing the benefits of such proposals, and incurring surprise fees and charges, this may act as a strong deterrent to allow other industry and regulatory initiatives in gaining traction.

Equally, the Bank, rather than relying on industry commitments, may require the invocation of its regulatory powers, to ensure the industry participants comply with providing LCR capability to its merchants.

Q6: Is there a case for further policy action to enhance competition in the provision of acquiring services to merchants? If so, what form could this action take?

It would be advisable for the Bank to review the UK's Payment Systems Regulator's (PSR) Interim Conclusions Report, due, Q1 2020, on its review of card acquiring services, to consider and draw upon any recommendations put forth by the PSR, which the Bank can benefit from. In doing so, potentially fast-tracking findings from the PSR's Conclusions Report which the Bank deems consistent and applicable to Australia's merchant acquiring services. Thereby saving the Bank valuable resourcing time, cost, and effort were it to start such a particular process from the beginning.

Q7: Is there a case for greater transparency in scheme fee arrangements, including their effect on payment costs? If so, what form should this take?

An independent study by a consulting firm that works with UK retailers, acknowledged that since the implementation of the Interchange Fee Regulation (IFR), scheme fees accounted for 30 per cent of merchant service fees passed on by acquirers[8]. However, we need to appreciate that if interchange fees fall, while scheme fees remain relatively static, by this virtue, the percentage of scheme fees to aggregate merchant service fees will rise.

Notwithstanding, scheme fees were a key topic of review by the UK's PSR, where the PSR acknowledged lack of transparency around the fees merchants pay to accept cards[9]. It may further benefit the Bank to consider if larger acquirers and/or merchants stand to gain from scheme fees.

And if the Bank can identify that if larger merchants are able to use their scale to negotiate lower scheme fees with their acquirers as part of their overall merchant service fees, should the Bank further determine if smaller merchants are subsidising this benefit.

Which could possibly lead to smaller merchants being faced with a higher than average reasonable cost of accepting card transactions, potentially leading to a higher price for their goods and services.

In which case, the Bank may consider whether graduated regulation is required, or regulation ensuring consistency in the transparency and application of scheme fees on merchants within the market, irrespective of their size.

Q8: Are the existing access regimes working effectively?

No feedback is provided at this stage.

Q9: What are the implications of the growing importance of mobile devices and digital platforms for the retail payments system in Australia? Are there issues that arise for the Bank's regulatory regime for card payments or that are relevant to competition, efficiency and risk?

---

[8] In Depth: *Which? Warns of 'Market Failures' As Card Schemes Strengthen* - paymentscompliance.com, 19 July 2018. Basquill, J.

[9] PSR MR18/1.2 - Final terms of reference: market review into the supply of card-acquiring services - psr.org.uk. Published 24 January 2019

Card Regulation Pertaining to Interchange

With the ever rising reliance, as well as the growing centralisation of services to mobile devices, and the innovation provided by digital platforms, these factors all speed up the growing infrastructure of Australia's retail payments systems, networks and interconnectivity, and the reliance for telecommunications providers' networks to maintain business continuity.

As mobile devices operate on telecommunications networks, there is the added dependency and risk that if a telecommunications provider's network sustains an incident, this may result in extended disruptions to mobile payments, mobile banking, and push/pull (incl. two factor authentication), and other services attached to digital wallets.

And the Bank may be caught in a predicament where the payments system is disrupted by organisations which it has little, if any regulatory enforcement over, **and possibly results in a systemic incident affecting millions across multiple institutions**. The Bank, and possibly with the assistance of other regulators, will need to be mindful in monitoring the current and evolving landscape of developments in these payment technologies and oversee that any regulation underpinning this infrastructure, is aimed at strengthening operational resiliency in payments.

Further in terms of regulation, and given that a card's credentials can be stored and transacted using a mobile device, whether the card's credentials are stored in a secure element, or accessible via host card emulation, the Bank may need to consider how it applies regulation across the grey area between a physical card, and virtual card. Which may extend to interchange for example.

In that, as more customers use digital devices to facilitate retail payments, especially as user functionality and on-boarding increases via the NPP, it is envisaged that issuers will issue fewer physical cards. In Australia, between October 2017, and October 2019 inclusive, there was a reduction of just over 3.2 million credit and charge cards. And for the equivalent period, there was a reduction in approximately 2.5 million debit cards[10]. A total reduction of over five and a half million physical plastic cards in force during this period.

Appreciating that a fundamental premise for the establishment of interchange was to balance the cost of card issuance, and if fewer physical (plastic) cards are being issued over time, there arises a valid point on whether interchange can in fact be further reduced, to adjust for lower issuance costs incurred by issuers brought on by fewer cards in force in the market. Given banks can now issue virtual cards directly to their customers' mobile devices and have been doing so for some time.

Recognising that for an issuer to issue a plastic card, below are just a few of the costs incurred from initial design and scoping, to final issuance and transaction by the customer. Therefore, a reduction in any of the below costs brought on by issuers issuing fewer physical plastic cards, all contribute to lowering their aggregate costs of card issuing.

Sourcing of plastic	Sourcing of the smart (EMV) chip	Artwork and design
Programming the chip/applets	Embossment	Security features[11]
Application of scheme artwork	Testing of the card	NFC capability
Staff & technology expenses	Infrastructure expenses	Logistical expenses

Table 1: Card issuers' costs of issuing physical plastic cards.

[10] RBA Payments Data

[11] In the UK for example, scheme cards have, across the front face of the card, a security watermark (Mastercard uses **MC**, Visa uses **VISA**, and American Express uses, **AMEX**), that is only visible with use of ultraviolet light. This watermark is strategically placed at specific points on the front face of the card to further complicate forgery.

Card Regulation Pertaining to Mobile NFC Access

Recently, the German government, in response to its new AML CTF legislation coming into force this year, has mandated that electronic cash infrastructure owners to open up their platforms to others for a reasonable fee. Almost immediately, Apple responded negatively to this decision. A decision by the German government which appears to move against the grain of what the ACCC ruled in favour of Apple in 2017, when it denied four domestic banks from bargaining with Apple to access its proprietary NFC technology. To date, not all four majors fully offer Apple Pay to their customers, with Westpac due to implement sometime in 2020 for its own customers; while Apple Pay is currently available to customers of Westpac's subsidiary banks.

In light of this ruling by the ACCC, the Bank may consider how it views the restriction of NFC access by Apple Pay to industry participants, from the perspective of how this benefits, or, potentially limits participants from providing improved services to their customers. And if this is the case, especially if the German government's decision creates more tangible benefits to its payments system above the decision enforced by the ACCC on domestic banks, then does the Bank, as well as any other domestic regulators, need to further consider new, or amend existing regulation.

Q10: Is there a case for a further lowering of the credit or debit interchange benchmarks or any change in the way they are applied?

One consideration for which the Bank could further lower credit or debit interchange rests on the comments raised in question 9 of this feedback letter. These comments point to evidence that Australian card issuers are showing a continual trend in the reduction of physical cards being issued, potentially leading to lower issuance costs; a premise for which interchange fees were established and passed on by acquirers as revenues to issuers.

Contingent on which entity one sources views from, whether it be an issuer, a scheme or a regulator, card interchange has been established for multiple purposes. These purposes include, balancing the cost of card issuing, driving investment in innovation and fraud prevention, and funding rewards programs.

Outside the above comment, the Bank will need to carefully weigh potential impacts to customers flowing on from further reductions in credit or debit interchange. Such impacts could see even more reductions in customers' earn rates, potential increases in annual fees, and further caps and expiry dates on points redemption than prior to regulatory intervention to reduce interchange benchmarks[12].

Q11: Should regulation of interchange be extended to inter-regional interchange fees (i.e. interchange fees applying to transactions in Australia using foreign-issued cards)? What is the typical cost of transactions on foreign-issued cards, and how much of this is attributable to interchange fees?

The introduction of regulation to include inter-regional interchange fees may create benefits yet, unwanted side effects.

[12] Credit card interchange fees guide - mozo.com.au

One side effect may result in foreign regulators applying similar regulatory reciprocal measures to domestic issuers, which may lead to increased fees incurred by overseas merchants to accept domestically issued cards, which, contingent on the country, may result in that foreign merchant applying a higher surcharge to accept foreign issued cards, which the Bank may be left with little regulatory enforcement to overrule.

However, one benefit derived can be where the Bank establishes a bilateral arrangement, or even multi-lateral arrangements with regulatory agencies in other countries or jurisdictions, which can result in inter-regional interchange fees lowering, or, increasing at a slower time interval than historically.

Q12: Is there a case for applying regulation to three-party card systems? What form could this take?

The European Court of Justice ruled that, when a three-party payment card scheme, such as American Express, issues card-based payment instruments with a co-branding partner ('the co-branding extension') or through an agent ('the agency extension'), it is considered to be a four party payment card scheme[13]. Therefore, EU regulation appears to consider a three-party scheme to fall under regulation applied to four-party schemes, in a given set of circumstances.

However, to extend regulation to three-party models irrespective of the conditions, or circumstances, including the strategy they employ to issue cards, appears reasonable. This would ensure three-party interchange fees (or similar fee structure) where they are higher than four-party schemes, would fall in line with caps applied to four-party scheme models. This may result in lower merchant surcharging to cover merchant's reasonable costs for accepting three-party card transactions. Which may then even lead to higher acceptance by merchants of three-party scheme cards. Although, one potential downside could result to the clawing back of rewards programs attached to three-party scheme cards.

On a general observation, it was noted that when the Productivity Commission (PC) issued its Inquiry Report into the Competition in the Australian Financial System, in June 2018, although in the context of three-party schemes, the PC did recommend regulatory intervention by the PSB and ACCC to further regulate merchant service fees.

Interestingly, approximately a month later, the UK's PSR published its initial Draft Terms of Reference into its Market Review into the Supply of Card-Acquiring Services, which also scoped the review to include fees merchants pay for card acquiring services.

Q13: Is the revised net compensation provision in the interchange standards working effectively?

A challenge residing around net compensation provision is that domestic issuers, and international scheme networks can operate using different accounting standards. Thereby, contingent on the accounting standard used by either party to provide its compliance report on net compensation to the Bank, may inadvertently distort its numbers, potentially creating a perceived risk of being in breach of net compensation provision.

[13] *A three party card scheme involving a co-branding partner or an agent is subject to the same restrictions as those applicable to four party schemes with respect to interchange fees.* Court of Justice of the European Union. Press Release No 12/18. Luxembourg, 7 February 2018.

When in fact, it may be subjective whether a breach of an interchange standard has actually occurred, owing to differing accounting methodologies applied. Including the booking, application, and timing and interpretation of receipt of any incentives, rebates, favours in kind, and/or cash flows, or other means of incentivisation.

In introducing net compensation provisions (i.e. the standards), the Bank needs to remain cognisant that this may pierce the long-standing commercial veil between schemes and issuers.

These long-standing commercial arrangements between schemes and issuers exist to allow both parties to gain further market share, revenue, and provide cardholders with improved innovation, among other benefits. And since the implementation of the standards, it appears this regulation has had an impact on revenues on offer by these commercial arrangements.

They are commonly entered into between an issuer and a scheme where if the issuer meets its contractual obligations, the issuer stands to, and rightfully enjoy revenues and rebates, among other benefits. The revenues, rebates and benefits on offer to issuers include:

1. Revenues paid by the scheme to the issuer in meeting or exceeding Domestic Gross Dollar Volume (GDV);
2. Revenues paid by the scheme to the issuer in meeting or exceeding International GDV;
3. Marketing incentives paid by the scheme to the issuer to launch and market a new feature, or new scheme card within a contractually agreed period;
4. Development incentives paid by the scheme to the issuer to reconfigure an issuer's systems to issue new scheme cards, or develop a new, or modify an existing feature of that scheme's card;
5. Sign-on bonus paid by the scheme to the issuer;
6. Conversion incentives paid by the scheme to the issuer for flipping part or all of its card portfolio branded in a competing scheme, or schemes, over to the scheme which the issuer has signed into a new contract with;
7. Core Scheme Service Fees Rebates - rebates offered to issuing banks by the schemes; and
8. Rebates offered to the issuer to utilise consultancy services provided by the scheme and further analyse their card portfolio to maximise the issuer's strategic objectives.

All the above revenues and rebates which can be enjoyed by the issuer can add up to multiples of millions, which the issuer has more flexibility in reinvesting in its card program and provide new payment technologies, product innovations and security measures, rewards and loyalty, and other cardholder benefits.

To limit this activity by virtue of limiting revenues, issuers may be faced with less financial means to achieve the abovementioned. If participants regulated by the Bank's interchange capping regime are meeting these requirements, or, where they occasionally fail to meet, but remediate within the Bank's required time frame, the Bank should remain content that this compliance measure is being observed by the industry. Without further need to regulate commercial arrangements that have been in place and allow issuers and schemes to benefit from revenues which are also reinvested in technologies, innovations and offerings which benefit cardholders. Therefore, it is one school of thought to implement regulation, and another to measure its effectiveness and any unintended impacts.

Q14: What enforcement mechanisms would strengthen observance of the net compensation provision?

No feedback is provided at this stage.

Q15: Is the surcharging framework working well? Are there any changes that should be considered?

In the Issues Paper (3.4 Surcharging), reference is made, *"If a business chooses to apply a surcharge to recover the cost of accepting more expensive payment methods, it is able to **encourage** customers to consider making payment using a cheaper option."* One could challenge this statement in that while the merchant may encourage customers to consider making cheaper payments, are merchants **influencing**, and even against the best interests of the cardholder, to use a payment method that is more suited to the merchant's financial needs, as opposed to the customer's aggregate benefit. Which based on the recent adverse media report provided in Question 5 of this document, highlights inconvenience imposed on cardholders.

Unless circumstances restrict, choice of payment method should reside with the cardholder, especially if they benefit from earning other incentives, including, rewards points and cash back or other offers provided by their issuer.

Separately, the Bank could ensure industries consistently apply surcharging. In the Issues Paper, even with Qantas reducing its surcharge caps, one could rightfully challenge justification on how it can continue to charge caps of up to AUD $11 for domestic trans-Tasman flights, and up to AUD $70 for international flights. Even with its revised percentages for these card payment types, surcharging remains rather excessive, and other industries could raise objection on why such high fees continue in the market.

This disparity in surcharging by Qantas, can be seen as going against the intended purpose and spirit of surcharging regulations. And may result in merchants who abide by surcharging regulations to express concern to the Bank, with the intent of leading to a more balanced outcome within the industry.

And while the Bank acknowledges Qantas' recent surcharging reductions in the Issues Paper, *"The result has been a very significant reduction in the surcharges applying to lower-value air fares."* The impact of Qantas' surcharging on mid-value and higher-value air fares, may not be so encouraging. For example, using Qantas' current surcharging rates, for debit card, an AUD $5,000 international air fare will incur a surcharge of $18.00. For a credit card payment made on the same air fare will incur a surcharge of $51.50.

Q16: Is there a case for policymakers to require that BNPL providers remove any no-surcharge rules, consistent with earlier actions in regard to card systems that applied such rules?

Merchants should be able to apply surcharging, whether they are generating noticeable incremental business revenues resulting from the BNPL model or otherwise. Another alternative, which does not necessarily require regulatory intervention, is for merchants to negotiate fees with BNPL service providers directly, especially through a collective industry association and secure lower BNPL merchant fees, given the demand for this consumer purchase model increases.

It would benefit the Bank to closely monitor this emerging payment option afforded to consumers, to ensure that there is an even balance in regulation of surcharging applied across both card payments and the BNPL schemes. To avert potential imbalances between the regulatory applications of surcharging for different retail payment options and ensure some level of consistency.

Q17: Are there potential enhancements to the Bank's regulatory powers and enforcement mechanisms that could improve the effectiveness of retail payments regulation?

The RBA appointed a dedicated resource in June 2012 to formally develop a framework for industry participants to report their significant operational retail payments systems incidents[14]. The Bank holds over 8 years' worth of formally collected and industry reported data on participants' operational significant retail payment systems incidents. And would not only benefit in sharing data amongst industry participants, however, requiring participants to publish their significant operational retail payments systems incidents on their websites.

This follows a regulatory requirement enforced by the UK's FCA on UK banks. Although the Bank collected incident reports prior to the commencement of the abovementioned dedicated resource, it was after June 2012, this dedicated resource established a formalised industry framework to not only collect data on industry operational retail payments systems **significant** incidents, but statistical collections which also reported industry lower level severity retail payments systems incidents[15].

Given banks have had considerable expertise in developing, decommissioning, integrating internal and, acquiring external systems, and for extensive periods, the fallback response of the architecture of legacy systems being too complex, and contributing to incidents, can appear to be a procrastinating reason in strengthening their payments systems, and an overused cliché.

Also, the current global heightened awareness of cyber-attacks, even on Central Banks, increases the need to ensure proper investment, talent, and knowledge transfer procedures are in place to build and operate optimally resilient and strengthened payment systems[16].

While the Issues Paper mentions the PSB has endorsed the Bank to work with the industry and APRA to develop a standard of operational performance statistics to be disclosed by individual institutions, this only creates a closed loop reporting mechanism. As opposed to the Bank developing and implementing regulatory requirements specific to retail payment systems resiliencies for industry participants.

[14] It is noted the writer of this document served in the Bank, in this capacity. During which, the writer developed the framework for industry participants to report their operational retail payments systems incidents and provided ongoing statistical data, among other related topics, to the Bank's Payments Policy department on operational retail payments systems incidents, which at times were fed through to the Bank's Payments System Board.

[15] One benefit of statistical collections, is that this afforded the Bank the opportunity to review if lower level severity incidents were manifesting over time towards significant incidents, and for the Bank to pre-emptively engage that participant and request information on how they would avert these lower level incidents from becoming significant.

[16] *Bangladesh Bank official's computer was hacked to carry out $81 million heist: diplomat.* Reuters. 19 May 2016. Gopalakrishnan. R., Mogato. M.

Something similar to what the UK's FCA, Bank of England, and Prudential Regulation Authority have initiated through an industry consultation process on building operational resilience[17].

As mentioned above, the FCA mandates UK banks to make public their operational retail payments systems incidents[18]. And further, the FCA and the PSR fined the Royal Bank of Scotland for an operational payment systems incident which caused extensive outages and disruptions to retail payments services[19]. These are further regulatory measures the Bank could consider in achieving operational retail payments systems resiliency across the Australian payments industry.

-Ends-

[17] *Building operational resilience: impact tolerances for important business services.* Financial Conduct Authority. Published, 5 December 2019.
[18] *BBC reveals high frequency of UK banking outages from data mandated by the FCA.* ComputerWeekly.com. 1 March 2019. McKenna. B.
[19] *RBS fined £56m over 'unacceptable' computer failure.* BBC. 20 November 2014.