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Review of Retail Payments Regulation
Reserve Bank of Australia
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FCA Submission to RBA Review of Retail Payments Regulation

Overview

The Franchise Council of Australia (the FCA) is pleased to make a submission to the Reserve Bank of Australia's Review of Retail Payment Regulation.

The FCA is the peak industry association for the $184 billion franchise sector in Australia. There is a franchise operating in almost every type of business category, with varying levels of complexity and market share. Prior to the onset of Covid-19, the Australian Franchise sector represented nearly 600,000 Australian jobs, with over 1,300 franchise systems underpinned by nearly 90,000 outlets. Around 40 per cent of franchising in Australia is represented in the retail sector.

Over 95 per cent of franchisees are small to medium businesses even though some represent major brands. The majority of franchisors are also small to medium businesses. It is these small and medium businesses that provide significant employment and stimulate economic activity throughout Australia. These thousands of franchise businesses across Australia create and sustain employment and will have a major role in contributing to Australia's economic recovery.

Retail payments regulation

The FCA is significantly concerned about the potential for Australian small business to suddenly face a sharp escalation in transaction fees for online and in-store sales.

Such is the level of concern on behalf of Australian small business, the FCA is collaboratively working with other national industry bodies to advocate for reform in this area that does not punitively impact small business, retailers and consumers.

Least Cost Routing (LCR) enables merchants to choose the lowest cost debit fee offering, to minimise their costs. To provide an industry analogy, essential services like energy and telecommunications are expected to offer customers a default low-cost option.

The introduction of LCR in Australia has been difficult, with obstacles and disincentives put in place to inhibit its rollout.

These new barriers include:

- moving from Multi Network Debit Cards (MNDCs) – which are necessary for LCR – to Single Network Debit Cards (SNDCs) using international schemes, whose fees are usually higher;
- not enabling LCR in mobile wallets, which is available in other markets, for what is an increasingly common form of payment in Australia; and
- the introduction of new fees that make it harder to access LCR in online payment channels.

The FCA notes that in its recent Retail Payments Regulatory Review consultation report, the Reserve Bank of Australia (RBA) makes clear that *"a widespread shift towards SNDCs could threaten the viability of LCR*" and that if eftpos cannot compete and potentially has to exit the market, this "*would result in a significant lessening of competitive pressure in the debit market and would likely result in an increase in both interchange rates and scheme fees, impacting all merchants"*.

Particularly at a time when many Australian merchants are on the road to COVID economic recovery, and most of them are classified as small businesses, the FCA is recommending the following course of regulatory action:

1) Multi Network Debit Cards (MNDCs) be properly entrenched in a regulatory sense to promote and ensure a fair and level competition field in Australia
2) Least Cost Routing (LCR) is made available as the default option for all merchants in all payment channels. This must include tap-and-go, mobile wallets and online transactions.

3) Full transparency of merchant fees.

The FCA supports the Pegasus Economics submission to this review that makes the following conclusions:

- Despite ignoring the recommendations of the Black Economy Taskforce, the House of Representatives Standing Committee on Economics, and the Productivity Commission to regulate for LCR, the RBA is essentially relying on moral suasion to facilitate the take-up of LCR. The RBA and PSB have received assurances in the past from participants in the retail payments system that have either partially – if not completely – been ignored or reneged upon. On this basis, it should impose an outcome rather an rely on moral suasion and the assurances of unenthusiastic and unmotivated participants.

- For financial institutions there may not be strong incentives for the continued issuance of DNDCs and the provision of LCR (Reserve Bank of Australia, 2019, p. 16). For card issuers, there may be incentives to negotiate exclusive single-network contracts with a scheme that offers higher average interchange fees and large upfront financial incentives – such as the international card schemes (rather than eftpos).

- The competitive tension created by LCR has seen the international card schemes reduce their total merchant service fees from an average of 0.63 per cent (of the transaction value) in the March quarter 2017 to 0.46 per cent in the March quarter 2021.

- The flip side of the potential savings to merchants from LCR is the potential loss of revenue for the international card schemes and card issuers. Under those circumstances, it would be understandable if there was not a lot of enthusiasm on the part of the major banks towards the rollout of LCR.

- Domestic card schemes can sometimes struggle to survive even where an activity-based approach is taken to regulation that seeks to create a level playing field.

- Support from scheme-owning banks for domestic card schemes can be undermined through international card schemes incentivising card issuers with higher interchange fees as has happened in parts of Europe.

- Another reason as to why domestic card schemes can sometimes struggle to survive is provided by the numerous competition and antitrust law investigations and proceedings that Visa and Mastercard are subject to around the world.

- The international card schemes currently charge small and medium sized merchants somewhere around 44 basis points more for debit card transactions than eftpos. If, following the exit of eftpos, the remaining international card debit schemes were to increase their merchant service fees by further 44 basis points, similar to what has happened in the UK, then this would increase net merchant service fees for small and medium sized merchants in order of almost $1.2 billion per annum.

Again, the FCA sincerely appreciates the opportunity to provide input to this important review. For further information on this submission please contact info@franchise.org.au

Sincerely

Mary Aldred
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