

# Strategic Review of Innovation in the Payments System

Submission by Australia Post

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# 1. Executive Summary

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Australia Post welcomes the interest and intent of the Reserve Bank of Australia (RBA) to seek feedback on its strategic review of innovation in the payments system, specifically concerning the rapidly changing retail payments market. The complexity of payment systems and diversity of market participants necessitates a process of wide consultation and Australia Post appreciates the opportunity to provide its views on the current payments landscape and how specific issues could potentially be addressed.

Australia Post holds a unique position within the Australian financial services landscape and provides essential services to a broad demographic of customers across the most far-reaching distribution network in the country. Consequently, Australia Post, through both physical and digital channels, plays a significant role in the retail payments space; as a retail merchant, banking and bill payment agent and payment facilitator.

Australia Post has noted behavioural patterns in consumer payments very similar to those captured in the RBA 2010 Consumer Payments Use Study. The decline in cash and cheque usage has been matched by an increase in card usage, particularly debit. Australia Post has also observed that some segments of customers continue to express a preference for cheques as a method of payment meaning cheques continue to represent a significant proportion of Australia Post's total transaction volumes. Given the important role cheques play for many businesses and consumers, their continued availability is essential to ensure social inclusion and equal access to payment services for all parts of the Australian community. Australia Post would therefore support industry initiatives that seek to improve the viability of cheque processing to potentially extend the life of cheques as a convenient method of payment.

Using the RBA objectives of an efficient payments system as a guide, Australia Post also notes that:

- Whilst current governance arrangements seem to adequately promote innovation, there would be benefits in broadening the representation of existing payments' governance structures such as APCA.
- There are a number of possible improvements to the current structure of clearing and settlement rules including the development of standardised messaging and data formats, expanded settlement periods and expanded reference fields in the Direct Entry (DE) system.
- There is a case for using hubs to improve efficiency, access and innovation, particularly for paper-based processing as cheque usage declines.
- Despite current developments, there continue to be gaps concerning the regular clearance of funds, affecting the immediacy of funds availability.
- There may be a need for the RBA to create an environment that fosters innovation from a broad range of industry participants rather than just relying on larger players to drive innovation. This is particularly important in light of limited progress in recent innovation initiatives.

Australia Post has considered its diverse roles as retail merchant, banking and bill payment agent and payment facilitator in compiling this response and comment is supplied where relevant to Australia Post's business. Convenience, security, accessibility and cost transparency are all important attributes to Australia Post customers and as the RBA considers how best to support these ideals, Australia Post would welcome any further opportunity to consult with the RBA in achieving these aims.

## 2. The Decline of Cheques

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### **Australia Post Response Addressing Questions 1-7:**

Recently, community and Government concerns about the availability of suitable alternatives to cheques caused the UK Payments Council to abandon plans to cease cheque clearing in 2018. Despite a similar decline in cheque usage in Australia, Australia Post continues to observe reliance on cheques by a large segment of the community (meaning cheques continue to represent a significant proportion of Australia Post's total transaction volumes) and in certain situations (for example where other payment alternatives do not exist). Accordingly it is important that cheques continue to be available and activities to accelerate the decline in cheque usage may not be warranted.

Australia Post believes in allowing customers' choice and not disadvantaging segments of the community that have limited access to other payment instruments or methods.

Australia Post also recognises the high and increasing fixed costs associated with cheques as a method of payment. To address this issue, Australia Post welcomes industry initiatives that seek to reduce the average/unit costs associated with cheque processing to potentially extend the life of cheques as a convenient method of payment.

Australia Post has already suggested ways to reduce the average/unit costs of cheque processing. One such solution is to consider and investigate options for value exchange based on data and the removal of requirements for paper or images to be exchanged back to ledger banks. The industry benefits in this regard would be significant and include:

- Cost Reduction (including that involved to move paper cheques);
- Speed to clear funds and associated benefits to consumers;
- Increased revenue for the banking industry from interest earnings; and
- Reduction in processing errors for missing details, dishonours, stale cheques etc.

Australia Post believes that decisions regarding the ongoing availability and use of cheques are most appropriately left to the industry and the individual payers and payees that are party to payment transactions, as these players are best placed to understand their customers' individual preferences of payment method. Given the significant volumes of cheques that Australia Post accepts and transports currently, Australia Post is ideally placed to be a key player in working with other industry participants to explore alternative cheque processing solutions.

As cheque volumes decline to a level that does not justify wide scale investment by multiple parties, a trusted, independent third party such as Australia Post could provide shared infrastructure to all Australians and their banks by utilising the existing money order system as a replacement for bank cheques.

## 3. Cash Replacement

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### **Australia Post Response Addressing Questions 8-9:**

Similar to cheques, customers continue to express a preference for using cash as a method of payment, particularly for low-value purchases. Australia Post believes there are a number of reasons why customers continue to favour cash above other convenient payment instruments, including:

- No hidden charges for customers at the time of transaction;
- Known and consistent value at all times;
- Anonymity in transacting;
- Debt accumulation concerns (credit cards);
- Perception of greater speed for low-value transactions;
- Distrust of electronic payment methods due to fraud concerns;
- Greater bargaining power due to the immediacy of payment; and
- High level of acceptance.

Many of the reasons are based on perception as opposed to immovable barriers, so they may not represent long-term impediments to the continued development and adoption of cash replacement products.

Australia Post believes that appropriate cash-replacement products are under consideration or being developed across the industry and there does not appear to be a case for public intervention specifically in this area.

## 4. International Models for Industry Governance

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### **Australia Post's Response addressing Questions 10-19:**

The RBA, APCA and PSB continue to perform an important role in setting the reform agenda for the payments industry. Australia Post feels that current governance arrangements adequately promote payments system innovation. However, Australia Post can see benefits in broadening the representation of existing payments governance structures or anticipated future governing bodies to include payment system participants, service providers and end-users. This approach would assist in ensuring the needs of stakeholders are adequately voiced and in turn drive innovation where these stakeholders are demanding it.

In considering the allocation of decision making authority around innovations to any new or existing body, Australia Post believes there are risks that excessive process or regulation may in fact create a barrier to innovation. As such, Australia Post would not support membership based governance structures making binding decisions around innovations at this stage.

However, if it were the preference of the RBA to introduce a mandate around innovation, then Australia Post would expect to see broader membership accompanying this introduction. For example, membership by payments service providers (such as the banks) would need to be balanced out by payments system users (such as end-consumers and merchants). Further, the inclusion of independent participants as members should be considered. Giving a broad mandate for decision making whilst maintaining the current membership structure may lead to a conflict of interest.

Australia Post suggests a staged approach if it is the RBA's preference to move to a mandated approach to innovation. The first stage may entail a broadening in membership of current or future governing bodies and the introduction of greater non-bank participation. Included in this stage may be an assessment of whether these initiatives were enough to produce the desired level of innovation. If an assessment was made that innovation was not occurring at sufficient levels, then the next stage could include consideration of mandatory decision making powers.

Whatever the RBA's preference, Australia Post would expect that broad consultation with industry members would be required before assigning any mandate.

Any such governing body should be encouraged to monitor payments systems operating successfully in other countries, so as to ensure the benefits of their experience are brought to Australia.

Given our unique position in the payments market (largest physical retail network in Australia, providing a wide range of convenient payment options to hundreds of thousands of customers per day), Australia Post would welcome the opportunity to participate in further policy making processes around the future direction of the payments system.

## 5. Structure of Clearing and Settlement Rules

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### **Australia Post Response Addressing Questions 20-25:**

Australia Post considers that there are a number of possible improvements to the current structure of clearing and settlement that could benefit both consumers and payments industry participants as well as leading to greater opportunities to innovate. These include:

- The development and support of a consistent standardised messaging and data format assisting in the reconciliation of information and settlement. This would support further innovation, potentially making the development of new products and services easier with the creation of a streamlined, common clearing and settlement process;
- More regular settlement periods occurring 7 days per week, benefiting both customers and market participants through faster clearing, assisting in accounting for Australia's multiple time zones and potentially decreasing the risk of operational issues on overall system liquidity;
- Expanding the reference fields in the DE system (from 18 to 60 characters for example) or the inclusion of multiple notation reference fields attached to payments which would greatly assist in reconciling payments and promote more efficiency; and
- Enabling non-bank market participants to access cleared funds through digital channels providing their customers with more choice to use non-card based payment methods outside of internet banking.

Australia Post believes that a minimum standard message type is a positive way to reduce the required effort in negotiating individual acceptance agreements, further promoting competition and encouraging new entrants. From an efficiency perspective, the minimum standard needs to be greater than the current standard to allow market participants to drive innovation.

## 6. System Architecture

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### **Australia Post Response Addressing Questions 26-29:**

Australia Post recognises that other markets around the world have used hubs as a tool to improve efficiency, access and innovation. Given this success, Australia Post supports the RBA's consideration of hub opportunities within the Australian market. The promotion of a hub for clearing may be beneficial within Australia, assisting to reconcile information to enable easier settlement. Hubs would be useful for both wholesale and individual distribution of clearing files/transactions.

The use of a Community Of Interest Network ("COIN") model is viewed as being the best practice model to promote innovation and account for different business, investment and technology cycles.

As a major processor of government, individual, business, agency and other payments (particularly cheque and paper based) we are in a unique position to assist in assessing the implications around the various hub options and would welcome discussions with the RBA in this regard.

## 7. Innovation Gaps in the Australia Payments System

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### **Australia Post Response Addressing Questions 30-32:**

Australia Post has a vast retail network that enables us excellent insight into the needs of everyday Australians. It is consistently found that innovation in the payment space is required to achieve our customers' objectives of:

- Accessibility;
- Value for service;
- Speed and ease of transacting;
- Mobility; and
- Security.

Australia Post believes that current governance encourages innovation within the Australian payments market. However, specific barriers to innovation exist concerning scalability, standards and technology.

With the evolution of user channel preference through technology innovation, the sector requires better and equal representation from both a broader base of retailers and end users moving forward, ensuring change and innovation are user led and sector wide.



## 8. Standards & The Transmission of Data with Payments

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### **Australia Post Response Addressing Questions 33-35 and 46-50:**

Australia Post recognises the potential benefits of new or improved standards including:

1. Reducing the reconciliation time within an industry;
2. Reducing risk through the pooling of like entities and tailoring of clearing requirements; and
3. Reducing operating costs through scale and associated efficiencies.

Noting the likely costs to payments industry participants and possible flow-on consequences to their customers (e.g. employers making payroll) Australia Post believes it would be necessary for the RBA to fully assess the anticipated benefits alongside the associated costs and implementation risks of any major change before proceeding.

New or revised standards may not be the only way to fill any perceived functionality gaps, for example completely new payment platforms or services could achieve the same outcome with lower costs and risks. Australia Post believes the RBA needs to allow adequate time and opportunity for such alternatives to develop before mandating on standards, perhaps through explicitly testing their likely availability as part of any cost-benefit study.

## 9. The Timeliness of Payments

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### **Australia Post Response Addressing Questions 36-41:**

With its vast physical network, Australia Post is often instrumental in timely distribution of funds during emergency situations; hence we recognise the importance of timeliness in the clearance of payments. For example, the government partnered with Australia Post outlets to instantaneously deliver cash to those affected by the Queensland floods.

Despite current developments there continues to be gaps around the regular clearance of funds. Australia Post certainly witnesses demand for shorter clearance cycles to account for weekends, public holidays and time zone differences. It is observed that the demand for payment options that provide instantaneous access to funds varies depending on the sector in question. Agency customers (particularly small to medium businesses where cash flow is integral for ongoing operations) tend to favour same day settlement. Same-day settlement of funds is a service Australia Post can provide with offerings such as Postbillpay. However, Australia Post typically does not receive these funds on a same day basis, subjecting the organisation to risk and reconciliation issues.

Multiple settlements would have a positive impact in facilitating faster availability of funds and act as an enabler for international and online commerce. In the short term, Australia Post feels multiple settlements would be an effective method to facilitate faster availability to funds.

Further, Australia Post would welcome consideration to remove the requirement for physical exchange of paper or images in cheque processing. It is anticipated this would reduce the clearance of funds by at least a day.

## 10. Mobile Payments

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### **Australia Post Response Addressing Questions 42-45:**

Australia Post sees that the potential for mobile payments is strong, utilising new and emerging technologies. However Australia Post does not see mobile payments as a significant alternative to cash and cheques in the next 5 years.

Australia Post expects expansion into Near Field Communications ("NFC"), mobile and assisted IVR along with an increase in the use of 'eWallets' or stored/authorised card details to allow more convenient and secure online payments on the move.

Technology development such as NFC may be hampered by lack of stakeholder coordination in the payments sector to drive change. However it is expected that the commercial benefits and competitive edge gained through innovation in this space is enough of an incentive to drive stakeholders to act.

Wide scale adoption of mobile solutions are likely to be assisted by participation of a trusted third party (for example Australia Post) who can combine components from Telcos, Banks and other service providers and maintain connections to customers and their identities via the physical post office network.

## 11. Future Trends

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### **Australia Post Response to Question 51:**

Australia Post is keen to see the RBA closely monitor the current payments landscape. There are a number of recent innovation initiatives (such as MAMBO) that have not progressed as originally envisaged. There may be a need for the RBA to create an environment that fosters innovation from a broader range of industry participants.