

# Submission to the Sunsetting Review Committee

## Review of the Operation of the Sunsetting Provisions in the *Legislation Act 2003*

7 July 2017

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### Introduction – overview of Reserve Bank’s role as rule-maker

The Reserve Bank of Australia’s functions relevantly include oversight of the Australian payments system and various statutes authorise the Bank to make legislative instruments for that purpose. Responsibility for the Bank’s payments system policy vests with the Payments System Board, one of the two Boards of the Reserve Bank<sup>1</sup>.

The Payments System Board’s responsibilities include ensuring that:

- the powers of the Reserve Bank set out in the *Payment Systems (Regulation) Act 1998 (PSRA)* and the *Payment Systems and Netting Act 1998 (PSNA)* are exercised in a way that, in the Board’s opinion, will best contribute to controlling risk in the financial system, promoting the efficiency of the payments system and promoting competition in the market for payment services, consistent with the overall stability of the financial system; and
- the powers of the Reserve Bank that deal with clearing and settlement facilities set out in Part 7.3 of the *Corporations Act 2001 (Corporations Act)* are exercised in a way that, in the Board’s opinion, will best contribute to the overall stability of the financial system.

Under the PSRA, the Bank has the power to designate payment systems if it considers that it is in the public interest to do so and to set standards and access regimes for designated systems. The PSNA provides the Bank with the power to, amongst other things, approve certain real-time gross settlement (**RTGS**) payment systems so as to give legal certainty to settlement arrangements and minimise the risks of systemic disruptions arising from those payment systems.

Under Part 7.3 of the Corporations Act, the Bank has a formal regulatory role to assess the extent to which the infrastructure supporting the clearing and settlement of transactions in financial markets is operated in a way that promotes financial stability. The Bank’s powers under Part 7.3 include the power to determine financial stability standards for licensed clearing and settlement (**CS**) facilities.

Relative to other Commonwealth entities, the Bank has a small number of current legislative instruments for which it is the relevant rule-maker.<sup>2</sup> Further, each of the Bank’s current legislative

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1 The other Board, the Reserve Bank Board, is responsible for the Bank’s monetary policy and the Bank’s policy on all other matters, except for payments system policy.

2 As at the date of this submission, the number of registered legislative instruments currently in force and for which the Bank is the rule-maker is 14. The Reserve Bank previously made a number of subordinate instruments under

instruments is presently subject to a specific exemption from sunseting.<sup>3</sup> The Bank's submission is made in that context and is therefore limited to aspects of the Review pertaining to sunseting exemptions.

## Retention of current Reserve Bank exemptions and objectives of the sunseting framework

The Reserve Bank strongly endorses the retention of the current sunseting exemptions as they apply to the Bank's legislative instruments and submits that those exemptions are consistent with the broader objectives of the sunseting framework. In particular, section 54 of the *Legislation Act 2003* recognises that in order to ensure that the sunseting framework remains flexible and fit for purpose, certain instruments should not be subject to sunseting, including where 'the nature of the instrument makes sunseting inappropriate'.<sup>4</sup>

During 2012 and 2013, the Bank undertook a comprehensive review of its then current legislative instruments and, through the Department of the Treasury, provided the Attorney-General's Department with detailed reasoning as to why it would be inappropriate for relevant instruments to be subject to sunseting. Broadly, the Bank's reasons included that the instruments are designed to be enduring and/or that commercial certainty would be undermined by sunseting. Those justifications continue to apply to the Reserve Bank's instruments and are consistent with the current policy criteria for new sunseting exemptions granted by the Attorney-General.

Notwithstanding the fact that the Bank's legislative instruments are currently exempt from sunseting, the Bank undertakes periodic reviews of those instruments (both on a formal and informal basis) in accordance with the relevant legislative framework and the Payments System Board's mandate.

We expand on these matters below.

## Approval of RTGS payment systems under the PSNA

The Bank has approved<sup>5</sup> three RTGS systems for the purposes of the PSNA – the Reserve Bank Information and Transfer System (RITS), the Austraclear system and the Clearing House Electronic Subregister System (CHES). In each case, the effect of the Reserve Bank's approval instrument is to protect transactions executed through the system from being unwound in the event of the external administration of a participant in the system – in the absence of that approval, the application of

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regulation 38 of the *Banking (Foreign Exchange) Regulations 1959 (FX Regulations)* for the purposes of lifting a number of broad capital controls imposed under the FX Regulations. However, those subordinate instruments ceased to be effective in practice on the repeal of the FX Regulations and were repealed with effect on 1 April 2017 under the sunseting provisions of the *Legislation Act 2003*. The Bank also made a number of sanctions-related instruments under the FX Regulations, which were revoked in 2012 following the transfer of responsibility for sanctions administration to the Department of Foreign Affairs and Trade.

- 3 There are certain legislative instruments which are not made by the Bank (and for which the Bank is not the rule-maker) but which the Bank is otherwise involved in the administration of. Some of those legislative instruments are not exempt from sunseting – e.g. the *Reserve Bank Regulations 2016*, made under section 89 of the *Reserve Bank Act 1959*.
- 4 Explanatory Memorandum to the Legislative Instruments Bill 2003, clause 54.
- 5 Each approval is given pursuant to subsection 9(1) of the PSNA.

Australian insolvency laws could undermine the irrevocability of those payments and create severe liquidity problems in the payments system.

The Bank submits that the RTGS approval instruments are an obvious example of where the nature of the legislative instrument is such that sunseting would be inappropriate. These instruments are clearly designed to be enduring and it would be inconsistent with the fundamental purposes of the PSNA (which include providing for legal certainty and settlement finality of RTGS payments) for these instruments to lapse through sunseting. In addition, as these instruments preserve the integrity of the arrangements between banks and other system participants for the irrevocable settlement of transactions in real time, commercial certainty would be undermined by the sunseting of those instruments.

### **Financial Stability Standards determined under the Corporations Act**

As part of the Bank's oversight of licensed CS facilities, the Bank has determined the Financial Stability Standards for Central Counterparties and the Financial Stability Standards for Securities Settlement Facilities (together, the **Financial Stability Standards**), which are designed to ensure that CS facility licensees identify and properly control risks associated with the operation of their facilities and conduct their affairs in a way that promotes overall stability in the Australian financial system.<sup>6</sup> As centralised financial market infrastructure, CS facilities constitute critical elements of the financial system and a failure of a CS facility to appropriately control the risks associated with its services could adversely impact the stability of the Australian financial system. In that sense, the Financial Stability Standards are of enduring importance as they provide a means for the Bank to assess whether licensed CS facilities are employing appropriate risk controls and other practices relevant to financial stability and it would not be appropriate for those standards to be automatically repealed by operation of the sunseting framework.

Further, the Financial Stability Standards are based on standards set by international bodies (the Committee on Payments and Market Infrastructures of the Bank for International Settlements (CPMI),<sup>7</sup> and the Technical Committee of the International Organization of Securities Commissions (IOSCO)). As a member of the CPMI, the Bank regularly reviews the need for changes to the Financial Stability Standards to reflect any changes to international best practice. In addition, in accordance with the Corporations Act, the Bank conducts periodic assessments<sup>8</sup> of the extent to which each licensed CS facility has complied with the Financial Stability Standards, and must submit a report on each assessment to the relevant Minister. That assessment process provides a further mechanism for regular review of the appropriateness of the Financial Stability Standards.

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6 The Financial Stability Standards are determined pursuant to subsection 827D(1) of the Corporations Act.

7 Formerly the Committee on Payment and Settlement Systems.

8 Under subsection 823CA(1A) of the Corporations Act, the Reserve Bank must do an assessment of any prescribed CS facility licensee at least once a year. As at the date of this submission, there are no CS facility licensees prescribed for the purposes of subsection 823CA(1A). However, in accordance with the Bank's policy on the *Frequency and Scope of Regulatory Assessments of Licensed Clearing and Settlement Facilities*, the Bank currently conducts annual assessments for each of the four domestic CS facility licensees (ASX Clear Pty Limited, ASX Clear (Futures) Pty Limited, ASX Settlement Pty Limited and Austraclear Limited) and LCH.Clearnet Ltd.

## Card payments regulation – access regimes and standards determined under the PSRA

In the context of the Bank's regulation of retail payment systems, the Bank has:

- determined standards relating to interchange fees and merchant pricing that apply to participants in certain card payment systems designated under the PSRA;<sup>9</sup> and
- imposed access regimes in relation to certain payment systems designated under the PSRA.<sup>10</sup>

Those standards and access regimes are subject to specific exemptions from sunseting under section 12 of the *Legislation (Exemptions and Other Matters) Regulation 2015 (LEOMR)*.

Notwithstanding the fact that standards determined and access regimes imposed by the Bank under the PSRA are exempt from sunseting, the Bank periodically reviews its standards and access regimes to ensure that they remain necessary and fit for purpose. Most recently, the Bank conducted a comprehensive review of card payments regulation over the course of a year and a half, which culminated in the release of a conclusions paper<sup>11</sup> and a set of revised standards, each determined on 26 May 2016.<sup>12</sup> The Bank's review was a comprehensive examination of the regulatory framework for card payments and involved extensive public and stakeholder consultation, consistent with the Bank's statutory consultation obligations under the PSRA. The Bank also varied the access regimes for the MasterCard and Visa credit systems, and revoked the access regimes for the Visa debit system, with effect from 1 January 2015 to reflect changes in industry structure and in ownership of the card systems. It revoked the access regime for the EFTPOS system on 1 September 2015.

In addition to formal reviews, the Bank regularly considers the appropriateness of its standards and access regimes through other informal mechanisms. For example, the Bank's Payments Policy Department monitors and reports to the Payments System Board each quarter on trends and developments in retail payments, as well as relevant Reserve Bank engagement in domestic and international policy research. Further, the Bank's staff have ongoing engagement with the card schemes, their respective participants and other stakeholders, including with Australian Payments Network Limited (formerly known as the Australian Payments Clearing Association), the Australian Payments Council (an industry coordination body for the Australian payments industry that engages directly with the Payments System Board) and the Payments Consultation Group (comprising of representatives of payments system end-users). Each of these processes provides a mechanism for the Bank to consider, on an ongoing basis, the effectiveness of its standards and access regimes, and any need for variation to, for example, address competition and efficiency concerns raised by developments in retail payment systems or through stakeholder engagement.

It is the Bank's view that the timing of review of its standards and access regimes should be driven by these processes, and by changes in industry, rather than by a fixed sunset deadline. Such a fixed deadline may trigger an additional burden on both the Bank and the industry at a time when their

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9 Each standard is determined pursuant to subsection 18(1) of the PSRA.

10 Each access regime is imposed under subsection 12(1) of the PSRA.

11 See the Bank's *Review of Card Payments Regulation – Conclusions Paper – May 2016* – available at: <http://www.rba.gov.au/payments-and-infrastructure/review-of-card-payments-regulation/pdf/review-of-card-payments-regulation-conclusions-paper-2016-05.pdf>.

12 See [Standard No. 1 of 2016: The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers](#), [Standard No. 2 of 2016: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers](#) and [Standard No. 3 of 2016: Scheme Rules Relating to Merchant Pricing for Credit, Debit and Prepaid Card Transactions](#).

respective resources are better spent in other activities. In addition, with the passage of legislation enabling the ACCC to take action in relation to excessive surcharges imposed by merchants, the Bank's standard on merchant pricing is now referenced in Commonwealth legislation: a fixed sunset deadline would create uncertainty for the ACCC and for businesses seeking to comply with their obligations in relation to surcharging.

## Purchased payment facility exemptions – declarations under section 9 of the PSRA

Under subsection 9(3) of the PSRA, the Reserve Bank is able to declare that specified facilities, or classes of facility, are not 'purchased payment facilities' for the purposes of the PSRA. The Reserve Bank has made three such declarations to date covering loyalty schemes, gift card facilities, electronic road toll devices, pre-paid mobile phone accounts, limited-value or limited-participant facilities and a specific insurance card facility.

These declarations allow non-Authorised Deposit-taking Institutions to operate facilities of limited scope without the need for authorisation and regulation under Part 4 of the PSRA. As such facilities pose a negligible risk of disruption to the broader payments system, regulating their activities would impose additional costs without providing significant public benefits. It is appropriate to exempt declarations under section 9 of the PSRA from sunseting because they have a significant impact on long-term commercial decisions. They provide operators of facilities with certainty that they will not be subject to additional regulation. If declarations were to lapse through sunseting, these facilities may face significant additional compliance costs and uncertainty as to whether they were able to benefit from a further declaration or alternative form of exemption.

In response to a recommendation of the 2014 Financial System Inquiry, the Reserve Bank and other relevant regulators will be undertaking a review of the regulatory framework for purchased payment facilities in the near future that will likely include a review of the current declarations under section 9 of the PSRA.<sup>13</sup>

## Determinations under the Cheques Act

Under subsection 70A(4) of the *Cheques Act 1986* (the **Cheques Act**), the Reserve Bank is able to determine, by legislative instrument, that a cheque settlement system is 'recognised'. Recognition makes it clear that a financial institution can reverse a provisional credit for a cheque deposit in the event that the institution on which the cheque is drawn cannot settle. The Reserve Bank has made one such determination in 2004, in respect of the Australian Paper Clearing System. It is appropriate to exempt determinations under section 70A of the Cheques Act from sunseting as they are of enduring importance. They provide legal certainty as to the enforceability of rules concerning the reversal of provisional credits in cheque systems. If determinations were to lapse through sunseting, financial institutions may be exposed to liabilities with respect to cheques drawn on failed institutions.<sup>14</sup>

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13 See Recommendation 16 in: [http://fsi.gov.au/files/2014/12/FSI\\_Final\\_Report\\_Consolidated20141210.pdf](http://fsi.gov.au/files/2014/12/FSI_Final_Report_Consolidated20141210.pdf)

14 Despite the declining use of the cheques system (on average, Australians made fewer than 5 cheque payments per person in 2016 compared with around 45 per person in 1995), it is worth noting that cheque settlement values are still significant – the value of cheque payments in 2016 was around twice the value of payments in the credit and debit card systems combined.

## Source of current exemptions and policy criteria for granting new exemptions

The Bank supports the retention in the LEOMR of the existing specific exemptions discussed above. In terms of its possible need for further exemptions in the future, the Bank believes that the five policy criteria continue to be appropriate. They have enabled the existing exemptions discussed above to be made, and have appropriately recognised the need for enduring commercial certainty.

The Bank does not have a strong view on whether the criteria for applications to the Attorney-General to grant new specific exemptions from sunseting should be set out in legislation, rather than policy. On this issue, the Bank makes the following brief observations:

- although the Bank recognises the need to retain flexibility in the application of the sunseting framework, rule-makers should generally have certainty as to the relevant criteria for granting exemptions at any given time; and
- any proposed changes to the criteria (particularly the removal of an existing criterion for granting of an exemption) would ideally be subject to a consultation process with affected Commonwealth entities.

Reserve Bank of Australia  
7 July 2017