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28 March 2019

Dr Tony Richards  
Head of Payments Policy Department  
Reserve Bank of Australia  
GPO Box 3947  
Sydney NSW 2001



By Email to: [PYSubmissions@rba.gov.au](mailto:PYSubmissions@rba.gov.au)

Dear Dr Richards,

### **Consultation on “The Operation of the Interchange Standards, February 2019”**

Commonwealth Bank of Australia (CBA) appreciates the opportunity to contribute to this consultation. CBA supports in principle the majority of the proposals in the Consultation Paper. We agree that greater clarity about the interpretation of the standards will be beneficial to improve understanding of, and compliance with, our obligations. However, we have concerns that the drafting of the amended standards, in attempting to increase clarity, could now be interpreted as unintentionally restrictive. We predict challenges particularly in relation to issuers partnering with or entering into arrangements with schemes in relation to non-core value-add services, as schemes increasingly compete with other service providers in expanded lines of business. CBA would be happy to provide case studies to illustrate these issues when we meet with the RBA on 2 April 2019.

CBA considers that the ‘incentive test’ should be stringently applied when considering the relevance of fees, payments, ‘pass throughs’ and other forms of benefits to avoid capturing unrelated transactions which could lead to the unintended consequences of hindering efficiency and competition in the Australian payments system and related markets.

CBA estimates that the implementation and ongoing reporting of compliance with these Standards annually would amount to approximately 82 hours of additional work across Compliance, Finance, Risk and Senior executives.

The Issues Paper seeks the views of stakeholders on a number of proposals. These are addressed below.

**Proposal 1: *The Bank’s Standards No. 1 and No. 2 of 2016 would be modified to require an accrual approach to be used to allocate Issuer Receipts and Issuer Payments to, or between, reporting periods in a manner consistent with the purpose and intent of the***

**standards, such that in determining net compensation certifying entities have more scope to draw on information from financial accounts prepared in line with generally accepted Australian accounting principles. Compliance would not be permitted on a cash or quasi-cash basis.**

CBA supports this approach. An accrual basis more accurately reflects the underlying commercial substance of the contractual arrangements. This is because the payments would be reported in the same period as the corresponding underlying transaction.

**Proposal 2: Clarify that 'Issuer Payments' are those payments made by issuers in relation to core services of a scheme.**

CBA in principle supports this recommendation however we have concerns that the wording of the definitions in Appendix A do not appear to reflect the intent of the changes as described in the Consultation Paper.

CBA appreciates the simplification of the proposed definition to restrict the standard to specifically 'payments' for core services and accepts the definition of Core Services as the 'minimum necessary services' for participation in a scheme. We agree that essential services should be distinguished from value adding options. However we do not consider that such services can be neatly classified into a discernible, standardised set of services assumed by the 'global provision test'.

CBA considers that the language in (c) of the definition of Core Services is open to an inadvertently prescriptive interpretation. Subsection (c), by imposing a 'global' standardised requirement appears to contradict subsection (a) which refers to the minimum necessary services for a participant in the Scheme in Australia. CBA therefore recommends subsection (c) is removed from the definition of 'core services'.

Additionally CBA suggests that this amended definition of 'core services' is applied uniformly to both 'Issuer Payments' and 'Issuer Receipts' to avoid creating a mismatch that could impact the outcome of the assessment.

**Proposal 3: Remove references to 'Acquirer' from the definition of 'Issuer Payments' in the standards.**

CBA supports Proposal 3.

**Proposal 4: Clarify the standards with the effect that where there is a price at which the supplier is regularly supplying relevant property or services, any discount or deduction from that price that meets the incentive test is a benefit to be included in Issuer Receipts.**

**Proposal 5: Clarify the standards with the effect that where property or services are supplied and there is not a price at which the supplier is regularly supplying the relevant property or services, the benefit to be included in Issuer Receipts, subject to the incentive test, is the amount by which the fair value of the property or services exceeds what is paid for the property or services (and if nothing is paid, then the full fair value is to be included).**

CBA accepts that there is potential for cards schemes to funnel value to issuers through discounts and non-financial benefits agreed or paid in relation to agreements for non-core services.

However, there is a risk that separate arms-length arrangements for non-core services could be included in the definition of 'Benefit' and therefore 'Issuer Receipts' which could lead to unintended consequences, such as reducing competition by schemes for such related services.

In particular, agreements between issuers and schemes relating to non-core services, such as loyalty programs, or platforms to provide customers with merchant-funded offers, may include pricing that caters for volume discounts or incentives to permit investment in start-up initiatives that may not be for the purpose of incentivising issuers to prefer that scheme's cards or encourage spend on those cards, but instead to grow the scheme's non-core services business. These discounts or incentives might however have an effect of increasing spend on that scheme's cards (e.g. if the issuer/s involved in the platform happen to issue mostly that scheme's cards). These discounts or incentives should not however solely for that reason be included in the definition of 'Benefit'.

CBA seeks clarification of the Standard to ensure that arms-length negotiated discounts or incentives are not inadvertently captured under paragraphs (b) or (c) of the definition of 'Benefit'.

In practice we consider that Proposals 4 and 5 will present a number of challenges. The standards refer to 'list, standard, usual price' in an attempt to provide a benchmark from which a discount or reduction can be measured. However, in commercial reality there will be a number of difficulties in accurately quantifying such a 'price'. For example, economies of scale, first mover incentive considerations and bespoke service offerings that have been tailored to the needs of the Issuer would all make price comparison difficult.

Overly restrictive inclusion of payments, incentives or pass throughs within the definition of 'Benefit' may inadvertently give competitors of schemes an unfair advantage in negotiations with issuers, as well as further complicate accounting and reporting under the Standards.

**Proposal 6: Clarify that the types of entity that an issuer can receive an Issuer Receipt from include associated entities of scheme administrators, drawing on the definition of Associated Entity in the Corporations Act 2001.**

CBA in principle supports the RBA's proposal to narrow the definition of Issuer Receipts to include only benefits provided directly or indirectly from a Scheme Administrator or any of its associated entities, with the definition of associated entity drawn from the *Corporations Act 2001*. For consistency we consider that a corresponding clarification should apply to Issuer Payments. However, CBA reiterates that the relevant benefits should only be included in Issuer Receipts if they meet the incentive test.

**Proposal 7:**

***The Bank's Standards No. 1 and No. 2 of 2016 would be modified, such that for scheme-issuer arrangements where one entity sponsors another for a card-issuing arrangement, it is only the sponsoring issuer that is required to comply with the net compensation provisions.***

CBA supports Proposal 7.

**Proposal 8: Provide transition arrangements that allow, for the reporting period ending 30 June 2019 only, an issuer to choose whether to comply fully with current standard or fully with the revised standard.**

CBA supports Proposal 8.

CBA would welcome the opportunity to discuss this feedback at the meeting with the RBA on 2 April 2019.

Yours sincerely

A handwritten signature in blue ink that reads "Michael Baumann". The signature is fluid and cursive, with a long horizontal flourish extending to the right.

Dr Michael Baumann  
Executive General Manager  
Everyday Banking  
Retail Banking Services

[ Signed ]