RESERVE BANK OF AUSTRALIA

A Strategic Plan for the Payments System

Submission to Treasury Consultation Paper

February 2023

Introduction

The Reserve Bank of Australia (the Bank) welcomes the development of a strategic plan for the payments system to help shape a shared vision of key priorities for government, industry and regulators.

The Bank supports the key principles that would underpin the strategic plan: efficiency, innovation, accessibility, and trustworthiness. As the strategic plan develops, it will be important for it to incorporate more information on specific actions and key milestones, to help inform industry investment and regulatory policy priorities. Inclusion of a clear roadmap and an annual review process will support progress towards the strategic priorities. The Bank looks forward to supporting this important work. This submission focuses on addressing consultation questions 3–5 on the key initiatives that could form part of the Strategic Plan.

Priority 1: promote a safe and resilient payments system

Reducing scams and fraud

The Bank welcomes the Government's focus on reducing the prevalence of scams and fraud occurring in the retail payments system. Payments-related fraud imposes significant costs on consumers, businesses and financial institutions, and can undermine public confidence in electronic payments.

Combatting rising scam activity and customer data theft have become a major focus for the payments industry and regulators over the past few years. The industry has been working with other stakeholders to better understand, detect and respond to possible scam activity conducted through bank accounts. It has also been seeking to raise customer awareness of scam risks and the ways people can protect themselves. The New Payments Platform (NPP) PayID addressing system is one method to help reduce the incidence of certain types of scams. This functionality allows the payer to check that the recipient's name matches their expectation, which can help the payer avoid being deceived into transferring funds to a scammer's account rather than that of the intended recipient. Although customer takeup of PayIDs has been rising, the Bank would like to see individual banks do more to promote greater use of them, including for account transfers involving businesses. Given the growing scale of the problem and the major impact that scams can have on people's lives, additional measures are likely to be needed in banking and payments (as well as in other sectors of the economy). The Bank will continue to engage with the Government, other regulators and the payments industry about initiatives to tackle payment scams.

Operational resilience in retail payments

Given the increasing importance of electronic payments, it is vital that entities in the retail payments industry invest in resilient systems and maintain reliable services for customers. Major disruptions or data breaches in these systems could have a material negative impact on end users and day-to-day economic activity, and significantly reduce public confidence in payment services and key providers. At the same time, operational challenges facing providers of retail payments are rising given greater complexity in payments infrastructure and services, and growing cyber threats. In 2019, the Bank implemented a new data initiative to improve the quality and transparency of information about retail payment service reliability. This involved enhancing the Bank's existing quarterly data collection for retail payments incidents, and requesting that individual payment service providers publish quarterly statistics on the reliability of their services on their own websites.[1] The Bank will continue to monitor the data on retail payment service outages and consider whether further policy actions are needed to support the reliability of retail payment services provided to end users. The Bank also plans to publish quarterly operational reliability statistics for its retail payment settlement services.

Operational resilience in retail payments also depends on the underlying infrastructure and payment systems that facilitate payments. Operational problems at shared payments infrastructure could have a major impact on the electronic retail payment system, since all payment providers offering these services to customers would be disrupted at the same time. Accordingly, the Bank has been assisting the Department of Home Affairs to apply the government's new critical infrastructure legislative framework to the operators of critical Australian retail payments systems. The systems that have been prescribed as critical are the Mastercard debit and credit card systems, the Visa debit and credit card systems, the eftpos card system and the NPP. The framework imposes several new obligations on the operators of these systems, including a requirement to maintain a risk management program for the purpose of mitigating significant threats to the reliability and security of their critical infrastructure assets, including the risk of cyber-attacks. The Bank has been specified as the relevant Commonwealth regulator in relation to the payment system operators' risk management program obligations.

Regulation of systemically important payment systems

A key responsibility of the Payment Systems Board is to promote the safety and stability of payment systems in Australia. The Board plays an important role in the governance of the Bank's supervision of Systemically Important Payment Systems (SIPS). The Bank's Reserve Bank Information and Transfer System (RITS) is currently the only domestic SIPS.[2] Threats to the operational reliability or security of payment systems are growing and creating greater risk of disrupting economic activity and financial instability. There have been system outages in low-value systems that have disrupted activity across parts of the real economy. Given these developments, the RBA is planning to broaden its work on safety and resilience to include additional payment systems, including the NPP.

Priority 2: ensure regulatory framework is fit-for-purpose and promotes competition

The Bank strongly supports the inclusion of the key priority to modernise Australia's payments regulatory framework. The way Australians make payments has changed significantly since current

1 The disclosures are being made by a range of service providers, including large and smaller banks and more specialised payments providers. See RBA, '[Disclosures on Retail Payments Service Reliability]'.

2 The Bank also identifies CLS Bank International as a systemically important international payment system.

regulatory frameworks were put in place, and it is important that regulation is able to adapt to new developments as the payments system continues to evolve. Providing clarity on the key milestones in the reform process through the proposed roadmap will help promote stakeholder certainty about the timing of the various reform measures.

Modernising the PSRA and new licensing framework for Payment Service Providers

A key initiative in this regard is updating the *Payment Systems (Regulation) Act 1998* (PSRA) to capture the full suite of payment entities and systems that play a role in the payments ecosystem. This would enable the Bank to regulate a wider range of payment systems and participants if it were in the public interest (i.e. by promoting competition, efficiency and stability, as defined in the PSRA). The Bank also supports the Treasurer being provided with new ministerial powers to address payment issues that are outside the scope of the Bank's public interest powers, where that would be in the national interest. This would be consistent with the Treasury Review's recommendation that the new ministerial powers be designed to ensure that emerging payments issues that fall outside the scope of the RBA's mandate – e.g. issues of national security or consumer protection – are able to be regulated where it is in the national interest to do so.

Another key initiative is to introduce a new licensing framework for payment service providers (PSPs). Introducing a tailored licensing regime should help provide greater regulatory certainty and address some of the challenges faced by PSPs seeking to operate in Australia, including access to payments infrastructure (see below). The Bank notes in particular that the current regulatory arrangements for stored-value facilities (SVFs, or 'purchased payment facilities' under current legislation) continues to be a source of frustration for some businesses. There is growing interest in this area, notably from firms offering cross-border payment services, and the current framework is complex and subject to potential regulatory overlap. The Council of Financial Regulators' 2019 proposals for reforming SVF licensing arrangements, which were endorsed by the Treasury Review, would introduce a more streamlined and risk-based approach to SVF regulation. Consideration could be given to the Strategic Plan prioritising reform in this area as part of the Government's implementation of a new PSP licensing framework.

The Bank also supports further work on a regulatory regime for payment-related stablecoins. These stablecoins are a subset of stablecoin arrangements with features that are specifically designed to facilitate their widespread use as a means of payment in the economy (i.e. to function as a form of 'money') – in particular, the ability (or implied promise) for customers to be able to withdraw their funds on demand and 'at par' (full value) in national currency. The Council of Financial Regulators has noted that the risks posed to users of payment stablecoins can be similar to those posed by certain SVFs, including the risk of user losses due to failure of the issuer to meet their obligations (e.g. because of a failure to appropriately safeguard customer funds, illiquidity and/or insolvency). The Bank suggests including an action to consult on regulation of payment stablecoins as part of the forthcoming consultation on regulation of SVFs (as part of the new PSP licensing framework).

Access to payment systems

The Bank has a strong interest in ensuring that payment service providers have reasonable and competitive options to access payment systems when providing services to their customers. Many payment providers connect to payment systems indirectly through a sponsoring institution. While indirect access options suit many providers, some payment providers may prefer to participate directly in clearing and settling payments on behalf of their customers without reliance on another financial institution. Currently, some payment systems have access criteria that make it difficult for non-banks to gain direct access. Payment system operators often rely on the risk management requirements imposed on banks and their supervision by APRA to mitigate risks to the payment system and its participants.

The Bank is developing a set of common access requirements to help support access to payment systems, including access to clear and settle payments directly via the NPP. The intention is for these requirements to be incorporated into a new licensing framework for non-bank PSPs that the Government is working to introduce. The Bank supports the development of the new licensing framework and common access requirements as a way to reduce barriers to entry and promote competition and innovation in the payments system, while ensuring risks posed by participants within payment systems are subject to appropriate risk management. It will continue to engage with payment system operators, PSPs and other regulators as this work progresses.

Reducing small business transaction costs

The Bank strongly supports the Strategic Plan incorporating initiatives aimed at lowering the costs small businesses incur when they accept payments. Small businesses, on average, pay twice what large businesses pay to process the same transaction. While economies of scale explain some of this difference, they are not the full story. The Bank welcomes the Government's support of the Bank's 'least-cost routing' (LCR) initiatives. LCR is functionality that enables merchants to choose which card network is used to process debit card transactions, typically the network that costs them the least.

The Bank has set a number of expectations for the industry aimed at making LCR more widely available and adopted by businesses in Australia. The Bank notes the Government's support of the timelines the Bank has set for the industry to make LCR widely available for online debit transactions and for mobile wallet debit transactions. Modernising the regulatory framework for payments, including the possible expansion of the regulatory perimeter of the *Payment Systems (Regulation) Act 1998*, would help the Bank address any instances where parties fail to meet the Bank's expectations with regards to online and mobile wallet LCR.

The Bank is supportive of broader initiatives beyond LCR which could help to further reduce costs, especially those faced by small businesses. These broader initiatives include the potential extension of the Consumer Data Right (CDR) to merchant acquiring services (which may help merchants shop around for a better deal).

The industry's ongoing implementation of the NPP Roadmap initiatives, such as PayTo, could also create more competitive pressure on card payments system operators and participants to lower the costs faced by businesses. NPP's PayTo service is an important initiative because it provides a convenient and secure way for households and businesses to authorise third parties to initiate NPP payments from their bank accounts. This service can be used as a modern alternative to the direct debit system, and allow businesses and consumers to benefit from increased speed, information and transparency associated with these payments. PayTo could be used in a range of other payment scenarios, including for in-app and e-commerce transactions, funding digital wallets and paying e-invoices.

The Bank has been advocating for the payments industry to meet commitments made in the NPP roadmap to extend the platform's capabilities, and the Strategic Plan could also support the NPP's Roadmap milestones. While the PayTo service went live in June 2022 as scheduled, many NPP participants (including several of the major banks) were not ready to begin offering PayTo services to their customers by this date. In response, the Bank obtained assurances from the relevant banks that they will be ready to enable customer accounts to authorise PayTo agreements and respond to payment initiation requests as mandated in the NPP roadmap, by April 2023. The Bank is closely monitoring progress in the rollout and adoption of PayTo services.

Priority 3: alignment with the broader digital economy transformation

Explore the policy rationale for a central bank digital currency (CBDC)

The Bank welcomes the Government's support of the work to explore the case for a central bank digital currency (CBDC) in Australia. Though it is maintaining an open mind, the Bank's view to date has been that there is not (yet) a clear public policy case for issuing a CBDC in Australia.[3] This reflects that Australia already has a modern and well-functioning electronic payments system that is meeting the needs of end-users, and physical cash is still readily accessible for those that want or need to use it. Much of the functionality that a CBDC might offer could also potentially be provided by private sector solutions, such as through the issuance of well-regulated, reserve-backed stablecoins. Depending on how it was designed, a retail CBDC could also be disruptive to the financial sector, with the potential to undermine bank intermediation and increase the risk of bank runs in stressed conditions.[4] Nevertheless, the pace of change in digital payments means the Bank is continuing to explore whether a policy case for a CBDC could emerge in the future.

Our current research focuses on understanding the potential use cases and economic benefits of a CBDC in Australia. The Bank has commenced a research project with the Digital Finance Cooperative Research Centre (DFCRC) that involves allowing selected industry participants to test potential use cases for a CBDC using a limited-scale pilot CBDC that is a real digital claim on the Bank. The Treasury is involved in this project, including being represented on its Steering Committee. A report on the findings, including an economic impact assessment, is expected to be published around the middle of the year.

The results from this project will provide valuable input into further work the Bank is planning to undertake with the Treasury to better understand the policy rationale for a CBDC in Australia. The Bank considers that the Strategic Plan will be a good way to give prominence to this work and encourage broader debate and engagement between the public and private sectors on this important policy question relating to the future of money in Australia.

Priority 4: modernising payments system infrastructure

Maintain adequate access to cash

The Bank welcomes the proposed inclusion of cash access in the Strategic Plan.

The Bank's Review of Banknote Distribution Arrangements and the Report of the Regional Banking Taskforce identified some financial and operational impacts of the decline in transactional cash use on consumers, industry and the public sector. Australia is not alone in experiencing this trend, and the

3 Australia is not alone in this regard; no other advanced economy central bank has committed to issuing a general purpose CBDC.

4 See Jones B (2022), '[The Economics of a Central Bank Digital Currency in Australia]', Speech at 17th Central Bank Conference on the Microstructure of Financial Markets, Sydney, 8 December.

overseas experience suggests that changes need to be adopted pre-emptively to avoid the loss of cash infrastructure as the use of cash for day-to-day transactions declines.

Although transactional cash use is likely to continue to decline, cash is expected to remain an important means of payment, particularly as it is heavily relied on by some members of the community (typically those in regional/remote areas, the older age demographic, people of lower socio-economic status and those with limited digital connectivity and literacy). Cash is also an important back-up for electronic payment methods and is used as a store of wealth; this applies on a day-to-day basis but becomes particularly important in times of economic uncertainty, as was the case during the COVID-19 pandemic. Despite declining transactional use of cash, the value of banknotes in circulation has continued to increase relative to the size of the economy.

Accordingly, the Bank sees merit in the Strategic Plan providing a framework for managing the decline in the transactional use of cash in an orderly way given the importance of cash for assisting financial inclusion, providing consumers with a choice of payment mechanisms, and its role in adding resilience to the system and being a safety net in times of crisis. Recognising the objectives of financial inclusion and choice in the key priorities would help ensure that the principle of 'accessibility' is appropriately represented in actions under the Strategic Plan (e.g. the first priority could be reframed as 'promoting a safe, resilient and *inclusive* payments system').

Initiatives to support inclusivity could include education and awareness that focuses on building consumers' capacity to use the variety of payments mechanisms that are available in Australia. The Government could also adopt Recommendation 6 of the Regional Banking Taskforce to continue to support and improve digital connectivity and literacy in regional areas, via initiatives such as Better Connectivity for Rural and Regional Australia Plan and the 'Be Connected' program.

The Bank's view is there would be benefit in the Strategic Plan clearly setting out the Government's position on supporting cash availability in Australia. There is considerable work being undertaken by other finance ministries and central banks internationally in this area. This can help guide the public and private sectors on how to respond to the decline in the use of cash for day-to-day transactions. Additional actions in relation to cash access should include:

- articulating the roles and responsibilities of the Government, regulators and industry in maintaining access to cash, recognising that this may change over time as cash use evolves.
- clarifying the concept of 'adequate' cash access, for example developing a framework for assessing the adequacy of cash access.[5]
- releasing a government response to the recommendations of the Report of the Regional Banking Taskforce relevant to maintaining access to cash in regional areas. One example is the recommendation to undertake actions to enable those not currently using electronic forms of payment to be in a position to do so by improving digital connectivity and digital literacy. Such an action also has the advantage of helping to ensure that the payments system is inclusive, and does not unnecessarily exclude consumers on the basis of where they live, or their ability to understand or trust the various payment mechanisms.

5 Some of the factors could potentially include the distance travelled to access cash and the fee status of cash access.

Legacy infrastructure

The Bank supports the proposal for the Strategic Plan to help coordinate action between the public and private sectors on the transition away from legacy systems to more modern and efficient payment alternatives. This is important from the perspective of payments system efficiency as maintaining obsolete infrastructure imposes a cost on the payment system and economy more broadly.

In the case of cheques, there has been a very significant decline in cheque use over the past few decades, and the per-transaction cost of supporting the cheque system, which is already high relative to other payment methods, is continuing to rise. There will be benefits in winding up the cheques system soon given the high cost of maintaining it and the increased availability of electronic payment methods that can meet similar needs. Facing similar circumstances, a number of comparable jurisdictions, including New Zealand, have already moved to close down their cheque systems.

The payments industry in Australia has been pursuing efforts over the past few years to support a customer-led transition away from cheques. Financial institutions have an important role to play in assisting their remaining cheque users to transition to suitable alternative payment methods and providing reasonable notice of any plans they may have to transition away from providing cheque services.

In addition to the actions proposed in the consultation paper, we believe there are some specific actions that could be included in future iterations of the Strategic Plan that could support the orderly wind-down of the cheques system:

- Clarifying and/or modifying any remaining legislation that mandates or promotes the use of cheques, or that imposes obligations on financial institutions in relation to cheques.
- Encouraging and supporting government sector users of cheques to migrate to alternatives.
- Raising public awareness of the rationale for winding down the cheques system and promoting the use of payment alternatives.
- Clearly setting out the Government's position on the importance of eventually winding down the cheques system. It may even be appropriate for the Strategic Plan to specify an end date for cheques at some point to serve as a focal point for any remaining steps required to complete the transition.

The future of the Bulk Electronic Clearing System (BECS), otherwise known as Direct Entry, will also be an important strategic issue for the payments system over the coming years. BECS has been a safe, reliable and low-cost workhorse of the Australian payments system for many years, and is still heavily relied on by businesses and governments. However, BECS has various technical limitations that reflect the time when it was created, including a delayed settlement model and a restricted messaging format. The industry has since invested in newer payment systems such as the NPP that offer faster, more flexible and data-rich payment options.

Given the potential cost of upgrading and maintaining BECS, it is appropriate that the industry is currently discussing whether and how the system could be wound down and eventually retired. There are a number of significant challenges that would need to be overcome for this to occur, including ensuring there are viable alternatives for all of the transaction use cases currently served by BECS and that these alternatives are safe, reliable and low-cost. There would also be a lot of work required to support end users of BECS during the transition. Many businesses and government agencies have BECS heavily embedded in their payments processing systems, and so they would require adequate time and support to transition to more modern payments processes.

In the near-term, the Government's Strategic Plan could help in encouraging buy-in and coordinating decisions between all key stakeholders on a plan for the future of BECS. If a plan to retire BECS was agreed, it would likely be a complex, multi-year project that would require ongoing coordination and support from all stakeholders, including government. The Strategic Plan could play an important role in supporting this process.

Enhancing cross-border payments

As highlighted in the Strategic Plan, cross-border payments is another area of focus in the work to modernise payments system infrastructure. Internationally, traditional bank-intermediated cross-border payments are widely considered to be expensive, slow and opaque. Recognising these challenges, the G20 countries have endorsed an ambitious roadmap for making cross-border payments cheaper, faster, more transparent and more accessible.[6]

The Bank welcomes the Government's support of this major international effort to enhance cross-border payments infrastructure and arrangements. The Bank is contributing to this work through its participation in a number of international working groups responsible for aspects of the roadmap. It is also undertaking several key actions to encourage the adoption of new functionality and messaging capabilities for cross-border payments over the coming years, in consultation with Australian industry participants and other Australian regulatory agencies. These actions should, over time, improve the international interoperability of these payments and help deliver better outcomes for Australian customers.[7] They include:

- Communicating an expectation that NPP participants meet their commitment to provide the NPP international payments business service by 1 December 2023. This new service will help speed up cross-border payments coming into Australia, by enabling the final Australian dollar leg to be processed via the NPP.
- Contributing to the multi-year international work to transition messaging for cross-border payments from proprietary legacy formats to ISO20022. In time, the adoption of a richer, internationally harmonised messaging system for cross-border payments should lower costs and speed up payment times.
- Together with the Australian industry, exploring the economic, business and technical issues that would be involved with potentially linking up the NPP to fast payment systems elsewhere in the world, over a medium-term horizon.[8]

The Strategic Plan also observes that the South Pacific countries face particular challenges in relation to the cost and accessibility of payments and banking services. The Bank continues to work with South

6 The roadmap is a multi-year program of targets, milestones and responsibilities to address various frictions in wholesale and retail cross-border payment arrangements. For further details, see: https://www.fsb.org/2022/10/g20-roadmap-for-enhancing-cross-border-payments-consolidated-progress-report-for-2022/

7 In 2021–2022, the Bank participated in a collaborative project (Project Dunbar) exploring whether using a shared DLT platform for issuing multiple wholesale CBDCs could improve the efficiency, speed and transparency of cross-border payments.

8 Last year, Singapore and Thailand became the first countries to link up their fast payment systems. This arrangement has reduced costs to consumers and enabled them to receive their funds within minutes.

Pacific central banks on the development of their electronic Know-Your-Customer (eKYC) capabilities, as well as other opportunities to improve the region's access to financial services and cost-effective remittances.

Reserve Bank of Australia
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