



9 July 2004

Dr John Veale
Head of Payments Policy
Reserve Bank of Australia
65 Martin Place
SYDNEY NSW 2000

Dear Dr Veale

Designation of ATMs

Thank you for the invitation dated 11 June 2004 to provide our views on whether it would be in the public interest for the Reserve Bank of Australia (RBA) to designate the EFTPOS and ATM payments systems in accordance with the *Reserve Bank Act 1959* and the *Payments System (Regulation) Act 1998*.

This submission will address the Credit Union Services Corporation (Australia) Limited's (CUSCAL's) views on ATMs. CUSCAL's views on EFTPOS will be provided in a separate submission. This submission covers CUSCAL's views as both an ATM network provider and as an industry representative of the majority of Australia's credit unions.

Role of CUSCAL

CUSCAL is the industry body for the majority of Australia's 176 credit unions. The CUSCAL Industry Association represents 153 credit unions which hold over 80% of the sector's assets of \$30 billion. Credit unions play an essential role in Australia's financial services sector, providing banking and financial services to more than three and a half million members, and offering a genuine and community based alternative to the major banks.

Credit unions in Australia:

- are the main financial institution for 9% of the population;
- are mutuals, where members own the credit union in which they are customers;
- are focussed on delivering benefits to members and a common set of values and ethics which govern credit union operations;
- have strong records of protecting depositors' funds; and
- continually report strong service outcomes – research in 2003 showed more than eight out of ten members rated satisfaction with their credit union as "excellent" or "very good" compared with less than four in ten customers of major banks.

The Rediteller Network

CUSCAL is also the owner and manager of the credit union Rediteller ATM network.

Rediteller is a national brand with ATMs on the network being owned by both CUSCAL and credit unions participating in the network. Agreements between CUSCAL and ATM Owners specify the type, appearance and operational standards for all ATMs on the Rediteller network.

Credit unions access the payment system through CUSCAL, which:

- holds and negotiates interchange bilaterals with other interchange parties;
- operates the Rediteller and Redinet system;
- provides links to the payments system through its membership card schemes;
- operates a national ATM network for credit unions, which it owns, and on which it acts as the acquirer and settlement party for interchange with other ATM networks and card issuers. From the perspective of external networks, CUSCAL is the Acquirer and Card Issuer;
- credit unions often charge lower or no fees for foreign ATM access.

The Rediteller network comprises approximately 1,300 ATMs. Approximately 6% of all ATM transactions occur through the Rediteller network. Whilst this makes the Rediteller network one of the larger ATM networks in Australia, it is important to note that ATM ownership within the Rediteller network is extremely diverse. For example, approximately 64 credit unions that participate in the Rediteller network own less than 10 ATMs.

Existing Fee Structure on Rediteller ATMs

Under the existing Rediteller arrangements, network fees are paid by the card issuer to the ATM owner on all relevant transactions. CUSCAL as the network owner also charges a small transaction fee. Whilst these fees can be recouped from members, the majority of credit unions currently choose not to pass on the fee to their members or provide a limited number of free transactions.

Context for Payments System Reform

CUSCAL generally supports the RBA's efforts to reform payments systems in Australia. These payments systems include ATMs, EFTPOS, Visa Debit, Credit Cards and BPay.

However, our support is contingent on a concurrent reform process. Individual payments system reforms cannot be considered in isolation and the impact of reforms on institutions and consumers must be considered collectively.

As small financial institutions with a large card issuing base, credit unions and their members are disadvantaged by the current disjointed reform process. For example, the credit card reforms have progressed independently of reforms to the EFTPOS payment system. Accordingly, credit union members now pay more for credit card transactions but have not received the anticipated reductions from the reform of EFTPOS interchange fees.

Credit unions and their members were disappointed at the retailers cynical moves to appeal the original Australian Competition and Consumer Commission (ACCC) determination to set EFTPOS interchange fees at zero. However, disappointment fails to adequately describe our reaction to the Australian Competition Tribunal's decision to set aside the ACCC determination. In our view, this decision has thrown the payments reform process into disarray and significantly undermined the validity of the co-regulatory approach to payments system reform.

ATM reform

As you are aware, CUSCAL has been a long-term participant in the voluntary reform process instigated by the RBA, the ATM Industry Steering Group (AISG). CUSCAL has worked with other industry AISG participants to develop a workable ATM reform model that would meet the requirements of both the RBA and the ACCC and our credit unions and their members.

From the outset, CUSCAL has maintained that ATM reform should not unfairly disadvantage smaller financial institutions and their members. It is our clear view that the implementation of a "pure" direct charging model would severely damage the ability of smaller financial institutions such as credit unions to provide competitive ATM access, an essential banking service, to their members. Under a pure model, all credit unions would be required to direct charge all other credit union members for transactions on ATMs across the Rediteller network.

This would lead to the demise of small ATM networks and consequently a reduction in competition in the ATM market. There would also be a flow-on effect as credit unions would struggle to maintain, let alone grow, member numbers if they were unable to provide a basic banking service such as ATM access. CUSCAL and credit unions cannot see how a valid public benefit argument can be made under a "pure" direct charging model.

Consequently, CUSCAL and credit unions have worked hard with other AISG members to develop a model for reform that meets the competition and transparency aims of the RBA/ACCC joint study whilst providing an opportunity for smaller financial institutions to participate in aggregate ATM networks. The AISG model is discussed further below.

The AISG model

Under the AISG model, which has previously been discussed with the RBA, direct charging would be adopted for the majority of transactions in the ATM market. However, some limited opportunity under the proposal would exist for financial institutions to form aggregated ATM networks. Transactions on these networks involving member institutions would not be subject to a direct charge to the cardholder. These transactions would instead incur a network fee paid between the card issuer and the ATM owner. All transactions by cardholders from institutions that are not members of the aggregated network would be direct charged. Card issuers may also charge a fee to their cardholder for each transaction.

The AISG model would essentially mirror the existing relationships between institutions in the ATM market. For example, participating credit unions on the Rediteller network do not have bilateral arrangements with any other parties in the ATM market. All bilateral links that facilitate access to the ATM network are negotiated and held by CUSCAL. Under the AISG model, all transactions within the Rediteller network would be subject to a network fee whilst all transactions with institutions outside the Rediteller network would be subject to a direct charge.

To ensure transparency, the AISG model proposed that network fees on the aggregate networks would be set according to a cost-based methodology developed subsequent to review by external parties. The fee, whilst not directly paid by the cardholder at the time of the transaction, would be fully disclosed to the cardholder.

In CUSCAL's view, the AISG proposal has the following public benefits:

- It enables smaller institutions to continue to participate in the ATM market, thus improving choice and competition in the marketplace;
- It ensures that fees are more closely aligned with costs;
- It ensures that cardholders are provided with more information about fees than under existing arrangements;
- It ensures that regional and rural services, many of which are provided by credit unions and regional institutions, will continue to be provided cost effectively; and
- It continues the broad access arrangements currently in place for cardholders in Australia.

The Reform Process

Whilst the AISG has reached agreement on a workable reform model, CUSCAL has publicly stated that it no longer has confidence that the voluntary reform process will deliver reform. The decision on EFTPOS reform by the Australian Competition Tribunal throws uncertainty into the ATM reform process. With limited resources, CUSCAL and credit unions can no longer commit to the voluntary reform process.

To be clear, CUSCAL and credit unions would support the adoption of the AISG model for ATM reform. However, considerable doubt surrounds the likelihood of this model passing through the ACCC and Tribunal process. This is not, in our view, a reflection on the public benefit merits of the proposal.

Accordingly, in the absence of a workable ACCC process, CUSCAL believes that the RBA should review its reform proposals. Should the RBA believe that payments reform continues to have merit, CUSCAL believes that there is considerable public benefit in delivering certainty to smaller institutions and consumers. This certainty appears to be only deliverable through direct RBA action.

The public benefit of designation must be considered across the entire payments system. If a reform path is to be pursued, those reforms must not be allowed to proceed in a haphazard manner. For example, credit card reform without EFTPOS reform undoubtedly leads to one group of stakeholders benefiting at the expense of others, and in our view, at the expense of consumers generally. Similar examples are apparent in the Visa Debit and ATM reforms.

The regulatory arbitrage game being played out by some large institutions hurts consumers and has the most significant impact on smaller financial institutions that do not have the resources to withstand the uneven revenue impacts of non-concurrent reforms and that do not have equal presence in all parts of the payments system.

Conclusion

CUSCAL and credit unions believe that any reform of the payments system must occur concurrently. Reform of individual parts of the payments system cannot be considered in isolation.

In our view, the voluntary reform process for ATMs cannot deliver this certainty and accordingly, CUSCAL and credit unions can no longer support voluntary reform in the current environment.

Small financial institutions and their members need certainty and consistency and for payments reform to be delivered equitably across all payments systems. This will ensure that no group of stakeholders is unfairly advantaged through delays in the regulatory process.

In CUSCAL's view, the voluntary reform process has been successful in developing a workable reform model through the AISG. However, for the benefit of consumers, the RBA should now consider giving renewed impetus to the reforms through using its powers under the *Payments System (Regulation) Act 1998*.

We are available to discuss this submission and ATM reform generally at any time and would be happy to provide further information as requested by the RBA. In the meantime, if you have any questions regarding this submission, please do not hesitate to contact Mark Degotardi (tel: 02-8299 9053) or myself (tel: 02-8299 9046).

Yours sincerely

LOUISE PETSCHLER
Head of Public Affairs