

9 February 2017

Dr Tony Richards
Head of Payments Policy Department
Reserve Bank of Australia

Dear Dr Richards,

Dual-Network Cards and Mobile Wallet Technology Consultation Paper December 2016

Coles appreciates the opportunity to provide the Reserve Bank of Australia (**the Reserve Bank**) with this submission on the issues raised for consultation in the Dual-Network Cards (**DNCs**) and Mobile Wallet Technology Consultation Paper (**the Consultation Paper**).

Coles Group Ltd and its related entities (**Coles**) provide fresh food, groceries, general merchandise, liquor, fuel and financial services to more than 21 million customers on average each week through its store network and online platform. Coles has more than 102,000 team members and operates 2,431 retail outlets nationally.

Coles has a long term strategic focus on lowering the price of the weekly shopping basket for our customers who on average have a weekly budget of \$150 for a family of four to spend on groceries. This focus has led to 7 years of consecutive price deflation in the weekly shop.

Coles is a Member of eftpos Payments Australia Limited (**eftpos**) and appoints a Director to the board of eftpos.

As a large merchant and self-acquirer, that has a clear business objective of minimising transaction payment costs in order to reduce costs for our customers, Coles puts forwards its views in this submission as set out below.

Background

In 2012, the Payments System Board discussed various issues of concern with eftpos, MasterCard and Visa including competition, consumer choice and costs. In 2013, the Payment Systems board judged that regulatory intervention around these issues was unnecessary at that stage. The networks and the Reserve Bank subsequently agreed to address the Payment Services Boards concerns through a voluntary undertaking. Coles notes the following commitments from the voluntary undertaking:

“- not to prevent merchants from exercising choice in the networks they accept, in both the contact and contactless environments; and

- not to prevent merchants from exercising their own transaction routing priorities when there are two contactless debit applications on one card.”

Based on Coles’ understanding of the undertaking, relevant experience and insight, we provide in this submission a response to the following questions raised in the Consultation Paper:

1 and 2. The benefits to end users of choice of card/scheme in mobile payments and impediments

imposed by card schemes on mobile wallet provisioning of competing networks on dual-network card

3. The likely effects on competition and efficiency in the payments system if choice is prevented or discouraged

5. The effectiveness of the initial principles of the voluntary undertaking for dual-network cards

8. Developments in payment card technology

The Reserve Bank also seeks views on mobile wallet provisioning of competing networks. Within the areas noted above we have provided views on such provisioning of competing DNCs. Although Coles does not have direct involvement in provisioning, we believe the breadth of our expertise and participation in the industry gives us a valuable perspective on this matter.

Consultation Paper 1 and 2. The benefits to end-users of choice of card/scheme in mobile payments and Impediments imposed by card schemes on mobile wallet provisioning of competing networks on dual-network cards

Coles believes that greater intervention by the Bank is required to promote cardholder or merchant choice to ensure a cost efficient payments system.

Coles believes that the introduction of DNCs has provided benefits to cardholders by reducing the number of cards they need to carry and to issuers by reducing the number of cards on issue. This is consistent with the conclusions of the Reserve Bank as set out in the media release of 21 August 2013. "Issuers" in this submission means Australian card-issuing financial institutions that issue DNCs (**Issuers**).

When contactless transactions were introduced for physical cards, further efficiencies for cardholders and merchants alike were achieved by improving the time of a transaction at the point of sale.

However, an unintended consequence of this change on a DNC debit card in a contactless transaction was that consumers no longer exercised choice in selecting eftpos or the international scheme (Mastercard and Visa) resulting in a systemic shift of volume to the international schemes. The current software that performs contactless transactions only ever relies on the first priority present on the card to determine the scheme against which the transaction is processed. Accordingly, Issuers and the international schemes, in practical terms, dictate that their network is selected for contactless transactions in preference to the eftpos scheme as the secondary priority. This outcome increases the overall cost to merchants for card acceptance and is either directly or indirectly passed onto the cardholder depending on the merchant model (surcharging or via price of goods).

Coles believes cardholders should drive choice, or, in their absence, merchants (who are able to make rational choices that promote efficiency).

In Coles' view, consumers are likely to select "debit" or "credit" at the PIN pad based on their access to particular accounts rather than access to one network over another. To the extent that some cardholders are forced by the scheme arrangements to use the international scheme to process their transaction, but are indifferent as to whether their payment is processed by the international scheme or eftpos, this unnecessary increased cost is directly borne by merchants and, as previously mentioned, either directly or indirectly passed onto the cardholder.

We believe that where a DNC debit card is issued to the cardholder to access their bank account, cardholders would want this to occur at the lowest possible cost to them. As outlined above, most cardholders do not understand the pricing mechanics of the respective networks and therefore trust "the system" to ensure optimal cost efficiencies.

In summary, Coles is of the view that the emergence of DNCs has meant that in the case of DNC debit card

transactions, the consumer no longer chooses which scheme will be used as the payment method for contactless transactions. Instead, it is the international schemes and Issuers themselves that determine the routing. This lack of consumer (or merchant) choice has the potential to provide a poor outcome for customers over the long term, given the international schemes charge higher rates than eftpos to route transactions through their schemes.

Consultation Paper issue 3. The likely effects on competition and efficiency in the payments system if choice is prevented or discouraged

eftpos has for over 30 years provided a safe, convenient and efficient method of payment for the benefit of consumers and merchants. eftpos is owned and operated by Australian companies (including Coles) and Coles sees eftpos as an essential and valuable part of the payments landscape in Australia.

In 2016, Australian consumers performed more than 2.2 billion eftpos transactions worth more than \$138 billion at more than 900,000 eftpos terminals. Each day Australians make more than 6 million eftpos transactions.

Coles believes that the choice of eftpos as a low cost debit scheme network in Australia could be threatened if the limitations of choice by cardholders (or merchants in absence of the cardholder choice) persist. In the interests of competition we would seek to ensure the ongoing viability and relevance of eftpos. This will need to be achieved in the contactless environment and also as mobile wallet growth accelerates.

As choice by the consumer is removed for contactless transactions, we see a continued shift of transaction volume from eftpos to the international scheme debit products that is driving additional cost into the payments system.

The presence of eftpos provides a significant discipline to ensure the market remains competitive and in our view is integral to the ongoing stability of the payments system. Without eftpos and the source of competition it provides, an important Australian asset that delivers cost efficiencies would be lost.

Without the current eftpos scheme, the scale, scope and market penetration will be difficult for new technologies and entrants seeking to fill the gap to replicate. It is also difficult to envisage that they would be wholly domestically owned or grow to the scale of the existing international schemes, nor be able to match eftpos' cost efficiency.

Consultation Paper issue 5. The effectiveness of the initial voluntary principles for Dual-Network Cards

It is Coles' view that the voluntary undertaking has not been effective in addressing the original concerns around competition, consumer choice and costs. As previously mentioned, since the undertaking, Coles has observed a systemic shift in volume to higher cost networks and the options available in the undertaking for merchants have not been taken up.

We have summarised below our views on why this has occurred and, where applicable, options on how some of the concerns could be addressed:

- **Undertaking was confidential:** While we appreciate that confidentiality was an agreed condition, the lack of transparency of the undertaking has made it difficult for merchants and self-acquirers to rely upon the principles relevant to them.
- **Principles too high level:** The high level nature of the principles has meant they are open to interpretation and have left areas of significant ambiguity when you consider, for example, the application of merchant routing in a practical context. This has shifted the risk in applying the principles to those it was intended to help.

Consultation Paper issue 8. Developments in card payment technology

Coles notes that the Consultation Paper specifically addresses mobile wallet technology. We acknowledge the move by the industry to obfuscate valuable card number information with the implementation of tokenisation is an important move in protecting against data compromises and ensuring the trust of cardholders in the system is maintained.

We do, however, have concerns that international networks could impose further technical restrictions on allowing choice of network in a mobile wallet where access to a cardholders account is currently facilitated using their DNC. As we understand it, the only way an Issuer can provision a card to the Apple Pay and Android Pay mobile wallets is via a network token. In the case of a DNC, it is also understood that international networks could deem the card number on the front of the card – that is used as a mechanism to provision cards to the mobile wallet - as being their own and prevent other network tokens from being provisioned and thus nullifying the card's dual-network functionality.

Today, a physical card number is issued by the Issuer using a "BIN" issued by the international network which, when combined with the account selection, is then used to route to the appropriate network for forwarding to the Issuer for verification. This principle ensures that a single "card number" can facilitate multiple routing choices based on the account selection (if one is made available). There is a risk that if this principle is not maintained, then merchant choice as contemplated by the voluntary undertaking will be lost.

As the mobile wallet evolves to cater for tokenisation online, there is a risk that the technology constraints imposed by the international schemes in the contactless environment are extended to the online channel. We believe that just as regulatory intervention is critical in the contactless environment, it is also critical in the online and mobile wallet channels to protect choice and maintain a competitive option in eftpos.

Conclusion

In summary, Coles believe that to address the points made in this submission, greater intervention is needed by the Reserve Bank through the introduction of new standards that provide clear guidelines on acceptable behaviour with respect to DNCs. This would ensure that all parties in the payments system better understand their responsibilities, that ambiguity is removed and that parties would have confidence that they were acting in accordance with the standards.

The standards could be developed in consultation with industry to reduce any compliance or technical complexity that might add cost to the payment system, whilst still preserving the intent of competition and driving cost efficiency.

Again, thank you for the opportunity to provide feedback as part of this consultation process. We trust that the observations made in this submission are of assistance to the Bank and we would be happy to discuss with you further any of the matters raised.

Yours sincerely,



Nikala Busse
Head of Payments