

28 March 2019

Dr. Tony Richards
Head of Payments Policy
Reserve Bank of Australia
65 Martin Place
Sydney NSW 2000

PYsubmissions@rba.gov.au

Dear Dr. Richards,

Operation of Interchange Standards - Consultation Paper, February 2019 (Consultation)

eftpos Payments Australia Limited (eftpos), Australia's domestic debit card network and designated payment system, is pleased to be given the opportunity to respond to the Consultation.

eftpos agrees with the RBA that there is a public interest benefit to be derived from maintaining competition in payments and supports the RBA's desire to improve understanding to lower regulatory and compliance burden.

Executive summary

In summary, the key submissions from eftpos are:

1. An annual certification on a cash basis with a two year rolling reporting period would meet the objectives, not require wholesale changes to a regulation which is currently clearly drafted, remove ambiguity and provide flexibility if activities span more than one reporting period;
2. Using fees as published by the payment system to an issuer as the basis of calculating Issuer Payments will negate the need to define Core Services (which would require constant refresh to allow for innovation and may be open to misuse);
3. Any reference to Issuer Payments should exclude foreign exchange fees and other global service offerings as their inclusion provides an immediate competitive disadvantage to any payment system that does not provide those services. Their inclusion would not meet the objective of maintaining competition;
4. The method of calculation of Supplemental Services is appropriate although payments of third party fees for goods and services should also be included.

Rationale for and effect of Consultation

The RBA issued the interchange standards in 2016, providing more than two years for designated payment systems and issuers to gain an understanding of the standard, seek clarification of how it is to be applied and put in place the recording, accounting and reporting mechanisms to enable compliance with the standard. This Consultation comes after the first reporting period and despite clarifications provided by the RBA to various participants before the reporting period. The current standard is clear in its use of language, specifically references to issuer receipts "paid" rather than "payable". Therefore, it has to be assumed that this Consultation is in response to misapplication of the standard by some participants in their certifications or suggestions that the standard has not been complied with because of some ambiguity of language. This begs the question of why that misapplication occurred or why further clarification is now sought. Presumably that is in relation to incentives paid within the reporting period that did not meet the cash accounting basis of the current standard. As such, eftpos queries (1) the need to change the standard now, (2) what action has been taken to enforce the current standard and (3) why no enforcement provisions or clarity of the impact of non-compliance has been added to the new standard. eftpos submits that enforcement procedures and consequences should be added to the standard.

Proposal 1: Cash or accruals basis

eftpos agrees that a cash basis is the most simple and straight forward basis for the application of the standard, perhaps with some flexibility in respect of multi-year agreements. If the calculation remained a cash basis but the reporting period was a rolling two year period, albeit that Issuer Receipts should always be less than Issuer Payments for the relevant reporting period, that would meet both objectives and the intention of the regulation.

Reference is made on page 3 of the Consultation to the cash accounting basis being the most simple and straight forward to apply, with one exception relating to clause 5.2(e) said to be in respect of upfront payments which apply to more than one reporting period. The current and any new standard should be applied to all payments under existing and new agreements with participants required to comply with the current standard, with enforcement applying even if the payments have already been made.

It should also be recognised that clause 5.2(e) is likely to apply to any agreement between both the international card schemes (ICS) and issuers that have financial years that differ from the period from 1 July to 30 June. An accruals basis supports long term incentive agreements that apply to entities that have different financial years as it allows allocation of payments to be aligned to those financial years and allocated across reporting periods, ie Issuer Receipts can be manipulated to ensure compliance based on agreed adjustments to receipts and payments timings. Some participants, eftpos being one, have financial years aligned to the reporting period within the standard. This is why eftpos proposes a two year rolling reporting period.

Proposal 2: Definitions of Issuer Receipts and Issuer Payments

The Consultation sets out the rationale for regulating net compensation to Issuers, that is, to ensure that fees compensation to Issuers cannot be used to circumvent interchange regulation given that compensation has the same value flow effect as interchange and is subject to the same upwards pressure as interchange. eftpos submits that net compensation rules should apply to all payments across the ecosystem, including but not limited to Acquirers and Merchants, as they have the effect of masking the impact of the lack of price competition, to avoid cross subsidisation by payment systems between Acquirers and Issuers and between tiers of merchants.

Net fees that are or approach zero have the same effect as interchange. A lack of transparency of fees for merchants impedes competition. Pricing behaviours which have the effect of encouraging bundling and blending of rates and which render price differentiation obsolete can also have a negative effect on competition and efficiency in payments, for example, overly complex pricing, lack of transparency in pricing. Each of those methods has the effect of removing any point of price differentiation and obscures the price signals that could improve efficiency and competition in payments.

eftpos agrees that Issuer Receipts should not exceed Issuer Payments in the relevant reporting period and that all Issuer Receipts of any kind or value should be included in the scope of the regulation. Definitions allow scope for circumvention, so should be avoided in regulation that is intended to be all encompassing. If a definition is required, then eftpos suggests that the definition be to any scheduled fees as published by the relevant payment system from time to time to its Issuers (whether globally or not given that country specific fees are possible depending on the maturity of innovations and appetite of Issuers in the market) with a disclosure requirement to the RBA of all fees that applied to Issuers during the reporting period at the time of certification. Such a definition would provide an ability for the RBA to verify the certification. The calculation method of fair value of Supplemental Services would then be valid to be applied to any services that are provided at discounted fees, unpublished fees or for no consideration.

In any event, clarification should be provided about the scope of the Incentive Test. For example, are fixed infrastructure charges that apply to connection to infrastructure necessary for processing of transactions generated from usage of Cards included within the Incentive Test?

If the RBA is minded to persist with adding a definition of Core Services, then the following are examples of the nature of services which would be considered to be core to the function of a payment system as it operates within Australia – fees for card issuance or acceptance; connection to network for processing, tokenization and detokenization, IP rights of use (trademarks, BINs, tokens, card specs, terminal specs), testing and certification, processing, reconciliation and settlement and disputes and chargebacks. Care would be needed to ensure that any definition kept pace with changes to form factors, channels, technology and infrastructure,

rather than requiring update in arrears of any innovation. In any event, eftpos does not support the definition including any reference to a "global" offering, or foreign exchange, as that would give an immediate competitive advantage to international payment systems to the disadvantage of eftpos.

A non-exhaustive list of examples of supplemental services provided to support Issuers in Australia and which ultimately lead to support for card issuance, for which fair value calculations would be needed, include trademark licensing; consultation benefit; attendance at best practice, user group or member forums (domestically only if fair competition is to be maintained), travel, visits to suppliers/service providers (best practice tours), secondments, interstate flights for representative attendance, developments, product R&D, consumer research.

Proposal 3: Removal of references to Acquirer from the definition of Issuer Payments

eftpos has no view on the deletion of the reference to Acquirer from the definition of Issuer Payments.

Proposal 4: Clarification that a discount of a price and non-financial benefits that meet the incentive test is a Benefit

eftpos agrees that a discount of the price and non-financial benefits that meets the incentive test are Benefits and that the calculation of a fair value for that benefit should be based on the AASB.

Proposal 5: Fair value of property where no price for regular supply

eftpos agrees with the proposed calculation of value for a benefit provided without a price, should be based on the fair value of the benefit in accordance with the AASB.

Proposal 6: Issuer Receipts to include from associated entities

eftpos agrees with the proposal, save that true pass through payments for eg merchant funded loyalty should be excluded. The potential for circumvention which concerned the RBA in the Consultation could be dealt with through the above proposed published fee requirement and disclosure in the payment system certification of receipts from involved merchants.

Proposal 7: Sponsoring Issuers to comply

eftpos agrees with the proposal as the payment system visibility and ability to influence (if the payment system is to comply with the Competition and Consumer Act) rests at the aggregator or sponsoring entity level.

Proposal 8: New Transition Arrangements

Standards are issued in respect of all participants of a designated payment system. Therefore, both the payment system and any regulated participant must comply with the standard. Many long-term incentive agreements have already been entered into, according to publicly available materials including press releases issued by the ICS. eftpos submits that the standard should be applied to every incentive agreement, both those existing and new agreements, with certifications required to be provided for any payments already made or received since the standards became operational, in light of the comments above about clause 5.2(e) of the standard.

The election of how to comply appears to now rest with Issuers, rather than designated payment systems and could be different for the reporting period ending 30 June 2019 than for the reporting period ending 30 June 2020. As the large Issuers have already entered into long term incentive agreements with the ICS, this leaves open the possibility for an Issuer to apply the option most beneficial to the accounting practices of their ICS under those existing agreements and seek to impose that same accounting practice on eftpos for ease and to maintain consistency of application of the standard for the Issuer. For eftpos, that means that the compliance burden of potentially having to support both a cash and accruals basis of calculation and reporting for the same reporting period for different Issuers rests with eftpos. If that is the case, eftpos will potentially have to put in place mechanisms, all of which will be manual, to calculate and adjust the application of the standard, to match each Issuer's election (and consistent with an application of international accounting standards according to the interpretation of an ICS), rather than consistently with the manner in which eftpos accounts for the application of the standard and potentially inconsistently with its own application of the AASB. It would be preferable in eftpos' view for one method of calculation to be settled upon for all participants and applied by all participants for and from the reporting period ending 30 June 2019.

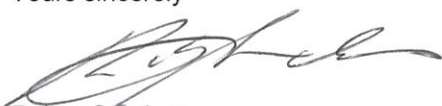
eftpos has assessed the compliance burden for the initial reporting period ending 30 June 2018 at approximately 3.5 days effort for one person. The estimated compliance burden of a changed standard as currently proposed, the effort would be 1 day for one person. This is due to the highly manual calculation effort required. If eftpos was required to support two different calculation methods in any one year, that compliance burden would be approximately 5 days effort for one person. For a cash basis with a two year rolling calculation and reporting period, the effort is estimated to be 7 days for one person. While the cost of compliance is a consideration, it is not the only or primary consideration. It is more important that the objective of the standard is achieved.

Draft changes to the Standards

eftpos has no comment on Standard 1. Attachment 1 contains suggested changes to the proposed new Standard 2, with explanations provided in comment boxed where needed.

eftpos would be pleased to meet with the RBA and discuss the submissions contained in this letter.

Yours sincerely



Robyn Sanders
General Counsel