

22 January 2021

Mr Scott Farrell,
Leader,
Payments System Review
The Treasury
Langton Crescent
PARKES ACT 2600

By email: paymentsreview@treasury.gov.au

Dear Mr Farrell,

Review of the Australian Payments System

COBA appreciates the opportunity to contribute to the Government's Review of the Australian Payments System.

COBA is the industry association for Australia's customer owned banking institutions (mutual banks, credit unions and building societies). COBA members are an important part of Australia's payments system, providing a wide range of payment products and services to their 4 million customers.

As noted in the Review Issues Paper, the payments system is regulated by a range of self-regulatory bodies, independent regulators – RBA, APRA, ASIC, ACCC & AUSTRAC - and the Federal Government. COBA members are:

- payments providers regulated by the RBA
- Authorised Deposit-taking Institutions regulated by APRA
- credit and financial services licensees regulated by ASIC
- Consumer Data Right data holders regulated by the ACCC, and
- reporting entities regulated by AUSTRAC.

COBA agrees that the payments system forms a central piece of Australia's economy and that the regulatory architecture should be structured to ensure the payments system best serves its end-users while boosting the productivity and efficiency of the economy as a whole. We agree that the regulatory architecture should encourage the development of secure payments technology that enhances user experiences, supports businesses through lower costs and empowers consumers with greater choice.

Key points:

Policymakers must consider the distinctive position of smaller ADIs when considering any reforms to payments system regulatory architecture. Ensure that regulators have a deep understanding of the existing payments ecosystem and the diversity and complexity of participants and their relationships and interdependencies.

The customer owned banking sector has engaged positively over a long period of time with the RBA as prime regulator of the payments system and the RBA has always given stakeholders an opportunity to argue their case and has typically allowed for appropriate implementation arrangements and transition periods when implementing regulatory change.

Reforms to Australia’s payments regulatory architecture should be considered against the following principles: allow the market to meet consumer needs, protect consumer confidence and minimise regulatory compliance costs.

Given that the payments system is subject to multiple regulators with different and sometimes competing policy objectives, ensure there is effective coordination, information sharing and mechanisms to reach balanced outcomes.

Customer owned banking sector

Collectively, our sector has \$144 billion in assets, 10 per cent of the household deposits market and more than 4 million customers. Customer owned banking institutions account for around three quarters of the total number of domestic Authorised Deposit-taking Institutions (ADIs) and deliver competition and market leading levels of customer satisfaction in the retail banking market.

Customer owned banking institutions are innovators and early adopters in meeting consumers’ evolving needs in payments, as demonstrated by our sector’s performance with digital wallets¹ and the New Payments Platform.²

COBA members provide their customers with a wide range of credit card and debit card products and, as a sector, we bring a card issuer and cardholder perspective to regulatory policy debates about payment cards. For example, our January 2020 submission to the RBA’s retail payments regulation review argued that our sector’s capacity to continue to deliver innovation and excellent customer service in consumer payments would be assisted by stability in regulation of interchange fees. Any further reductions in interchange fees would affect retail banking competition by having a disproportionately larger impact on smaller banking institutions who do not participate in the merchant acquiring market that is dominated by the major banks.

Credit card products issued by COBA members rate highly in comparison tests. Canstar found that:

- five out of the 12 low-fee credit cards rated as five stars for providing outstanding value are issued by COBA members, and
- five out of the 14 low-rate credit cards rated as five stars are issued by COBA members.³

A majority of COBA members are based in communities outside the major capital cities, serving regional Australia and playing an important role in facilitating access to the payments system for these communities.

As smaller players in a banking market dominated by the four major banks, COBA members rely on outsourcing to obtain efficiencies and economies of scale. This applies to core banking systems, data processing and other services but is particularly important in relation to access to the payments system.

The key providers of payments system access for COBA members are Cuscal, Indue and ASL. These providers’ services include participation in the international card schemes (Visa and Mastercard) and eftpos, the NPP, direct entry, BPAY, ATM networks, digital applications and cheque issuance.

¹ Apple Pay, Google Pay & Samsung Pay

² See speech by RBA Assistant Governor Michele Bullock 16 May 2019: “One of the positive aspects has been the broad participation of many small financial institutions. Customers of around 50 small banks, credit unions and building societies were able to make and receive fast payments from Day 1 and that number has since grown to nearly 70. On a less positive note, we have been somewhat underwhelmed by the progress of some of the major banks.”

³ <https://cdn.canstar.com.au/wp-content/uploads/2020/10/Crystal-Reports-Credit-Cards-2020-09.pdf>

Cuscal manages around 7.5 million credit, debit and prepaid cards on behalf of over 80 clients, many of whom are COBA members. CUSCAL provides services such as the issuance and management of cards on behalf of issuers, scheme sponsorship via Mastercard or Visa, card production and management, back office settlement, dispute resolution and compliance services, fraud risk management and access to digital apps.⁴

Indue provides support for COBA members in accessing the payments system. Indue's principal activities include the provision of processing, settlement and monitoring services in relation to financial access products including debit and credit cards, payments (NPP, BPAY, Chequing and Direct Entry – counter-party settlement, dispute management, stock production and transaction reporting).⁵

ASL's principal activities include the provision of settlement services for ATM/eftpos, Visa, Mastercard, direct entry, BPAY and NPP, as well as maintaining a risk management system and acting as a focal point for members to participate in the payments system.⁶

The interdependence between COBA members and third-party service providers is an important factor to consider when considering the overall regulatory architecture. Third party providers enable smaller issuers to manage technology and risk management costs, allowing for more players to participate in the payments market without compromising security or regulatory compliance.

Considerations for regulatory architecture

COBA urges the review to consider the distinctive position of smaller ADIs when considering any reforms to the payments regulatory architecture.

This requires a deep understanding of the existing payments ecosystem and the diversity and complexity of participants and their relationships and interdependencies.

Our sector has engaged positively over a long period of time with the RBA as prime regulator of the payments system, including in regulatory policy debates about credit card and debit card interchange fees and scheme rules and ATMs, and more recently on least cost routing and dual network debit cards and buy-now pay-later schemes.

In our view, the RBA has always given stakeholders an opportunity to argue their case and has typically allowed for appropriate implementation arrangements and transition periods when implementing regulatory change.

Any proposal to reform Australia's payments architecture should be considered against the following principles:

- first allow the market to meet consumer needs
- protect consumer confidence in the safety and security of payments system and their chosen payment method
- regulatory costs affect competition and are ultimately borne by consumers
- avoid a one-size-fits-all approach to regulation
- ensure regulation is tightly targeted at a clearly defined problem or regulatory objective
- seek to minimise regulatory costs, and
- recognise the impact of the cumulative regulatory cost burden, particularly on smaller banking institutions.

⁴ <https://www.cuscalpayments.com.au/cards/credit-cards/>

⁵ https://www2.indue.com.au/wp-content/uploads/2020/10/IND-3050-Indue-Annual-Report-2020_FINAL_Web.pdf

⁶ <https://www.asl.com.au/documents/annualReports/asl-annual-report-2020.pdf>

Balancing different objectives

As noted in the introduction to this submission, the RBA is one of multiple regulators responsible for regulating aspects of the payments system.

The various regulatory regimes have different and sometimes competing policy objectives that range from consumer protection to promoting efficiency and innovation.

ASIC is the consumer protection regulator in financial services and regulates payment product providers as financial services licensees.

ASIC also administers the ePayments Code, including monitoring compliance and conducting regular reviews. The ePayments Code “applies to consumer electronic payment transactions including ATM, eftpos, and credit card transactions, online payments, internet and mobile banking, and BPAY. Most banks, credit unions and building societies currently subscribe to the Code, along with a number of non-banking businesses.”⁷

Disputes related to the ePayments Code are handled by the Australian Financial Complaints Authority (AFCA). AFCA can consider complaints about payments, internet and telephone banking, including mistaken payments and secure payment system transactions.⁸

The ePayments Code is a critical piece of regulatory infrastructure in retail banking. Its key objectives include protecting consumers, promoting confidence in payments systems and providing clear and fair rules for allocating liability for unauthorised transactions.

COBA and other stakeholders are currently engaging with ASIC on a review of the ePayments Code. We have urged ASIC to move with great care and deliberation where proposals may affect the current levels of customer protection & customer responsibility and potentially increase moral hazard. An important consideration is the likelihood that any increase in the risk envelope, e.g. by extending the scope of the code or changing the liability provisions, will prompt a corresponding risk-management response from code subscribers that may negatively affect consumer experience.

In the context of liability for unauthorised transactions and disclosure of access codes, there has been ongoing debate about the practice of ‘screen scraping’. This can involve consumers handing over their banking credentials to enable third parties to access otherwise restricted interfaces.

The October 2020 Consumer Data Right Future Directions report⁹ noted that: “Given the risks of consumers handing over their banking credentials to third parties, the EU has prohibited screen scraping in relation to payment services, subject to transitional arrangements.” The report found that the eventual prohibition of the practice of screen scraping for payment initiation would be in the interests of consumers but this should only occur once CDR payment initiation is fully implemented as a viable alternative.

The report recommends that the CDR should allow consumers to authorise others to digitally initiate actions, such as initiating payments. The report further recommends that the ePayments Code should be updated to clarify how its liability provisions apply when a third party initiates a payment.

The CDR regime is complex, prescriptive and elaborate. It has three regulators, the ACCC, OAIC and a Data Standards Body. As of December 2020, Treasury also has a significant mandate, assuming responsibility for rulemaking “*to better enable the consumer data right to grow in a way that is*

⁷ <https://asic.gov.au/regulatory-resources/financial-services/epayments-code/#what-is-code>

⁸ <https://www.afca.org.au/make-a-complaint/banking>

⁹ <https://treasury.gov.au/sites/default/files/2020-12/cdrinquiry-accessiblefinal.pdf>

coordinated, accessible and secure {and} improve coordination of the ongoing expansion and operation of the regime.”¹⁰

Should the CDR become a payments mechanism, there is a case for the CDR regulators to have a voice at the Council of Financial Regulators (CFR).

Buy Now Pay Later (BNPL) providers pose another example of competing regulatory objectives in the payments system.

According to the RBA¹¹, BNPL providers charge merchants a “relatively-high” per-transaction fee, “often in the range of 3-6 per cent and is generally higher than the cost of accepting other electronic payment methods such as cards.”

Most BNPL providers also have rules that prevent merchants from levying a surcharge on the customer to recover those fees. The RBA notes that this may increase the cost of accepting payments for merchants that feel compelled to offer BNPL services as a payment option for competitive reasons but are unable to recoup the merchant fees from the customers that directly benefit from the service.

By helping to keep merchants’ costs down, the right to apply a surcharge means that businesses can offer a lower total price for goods and services to all their customers.

COBA’s view is that merchants offering BNPL arrangements should not be prevented from surcharging for this relatively expensive payment service.

While not directly relevant to retail payments regulation, stakeholders frequently comment on the fact that the responsible lending obligations in the National Credit Act do not apply to BNPL arrangements. This means that when providers decide whether to approve an application for an arrangement, they are not required to inquire into the consumer’s financial position, verify the consumer’s financial position or make an assessment as to whether the consumer would be able to repay the credit without substantial hardship. The “light” regulatory treatment of BNPL may be a factor in the rapid growth of the sector and is therefore a legitimate matter for consideration in an examination of payment system costs and competition and efficiency in the payments system.

Weighing up competing regulatory objectives in relation to BNPL, the RBA announced in December 2020 that it has adopted the “preliminary view” that:

“BNPL operators in Australia have not yet reached the point where it is clear that the costs arising from the no-surcharge rule outweigh the potential benefits in terms of innovation. So consistent with its philosophy of only regulating when it is clear that doing so is in the public interest, the Board is unlikely to conclude that the BNPL operators should be required to remove their no-surcharge rules right now.”¹²

A further example of competing objectives with respect to payments regulation emerged as a result of lockdowns due to COVID-19 and the rapid shift away from cash or in-person card payments.

Currently, section 992A of the Corporations Act 2001 prohibits the unsolicited offering of financial products to consumers. This measure aims to protect consumers from the hawking of financial products, which includes debit cards, unless requested by consumers.

In April 2020, the Federal Government urged all Australians, particularly those over 70, to self-isolate wherever possible, to curb the spread of COVID-19.

¹⁰ https://www.aph.gov.au/Parliamentary_Business/Bills_Legislation/Bills_Search_Results/Result?bId=r6633

¹¹ <https://rba.gov.au/payments-and-infrastructure/review-of-retail-payments-regulation/pdf/review-of-retail-payments-regulation-issues-paper-nov-2019.pdf>

¹² <https://www.rba.gov.au/speeches/2020/sp-gov-2020-12-07.html>

This left over half a million Australian bank customers, who use passbook or transaction accounts with no linked debit cards, with limited options to make transactions online or over the phone. Due to the Corporations Act provisions, ADIs were unable to proactively provide customers with alternative payment options.

COBA and the Australian Bankers Association (ABA) had to jointly seek relief from ASIC to fast track the issuance of debit cards to passbook holders as needed.¹³

While the positive outcome ultimately served the interest of consumers, this example demonstrates the complexity of overlapping regulatory regimes affecting payment products and their providers.

The CFR is comprised of Australia's financial regulatory agencies: the RBA, ASIC, APRA and the Treasury. The CFR's objectives are to promote stability of the Australian financial system and support effective and efficient regulation by Australia's financial regulatory agencies, recognising the benefit of a competitive, efficient and fair financial system.¹⁴

The CFR plays an important co-ordinating and information-sharing role in relation to the different regulatory objectives that exist across the financial sector and the various regulatory agencies. It allows agencies the opportunity to coordinate and provides visibility over workstreams that may overlap with other agencies regulatory mandates.

Importantly, the CFR is chaired by the RBA, enhancing its capacity to oversee the multi-faceted payments landscape.

This coordination and information sharing function is a critical consideration in any future changes to the regulatory architecture.

Giving the ACCC a permanent seat at the CFR may be desirable given the ACCC's role as CDR regulator and more broadly as competition regulator. As noted in the Review's Issues Paper, there is an ongoing need for co-operation between competitors "to develop shared protocols for initiating, clearing and settling payments, to respond to new developments and resolve issues."

Thank you for taking our views into account. I look forward to seeing your report. Please do not hesitate to contact Luke Lawler (llawler@coba.asn.au) or Maryanna Vasilareas (mvasilareas@coba.asn.au) if you have any questions about our submission.

Yours sincerely,



MICHAEL LAWRENCE

Chief Executive Officer

¹³ <https://www.customerownedbanking.asn.au/news-and-resources/media-releases/cards-help-vulnerable-customers>

¹⁴ <https://www.cfr.gov.au/about.html>