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Other matters

Payment system reform

Credit card fees

- 3.1 **According to the RBA, credit cards are, for both cardholders and merchants, the most expensive way of making a payment. At both the Brisbane and the Sydney hearings the Governor noted that the banks make greater profits from credit card transactions than cash, cheque, EFTPOS or direct credit transactions.**
- 3.2 In spite of this, credit card payment remains the most popular form of payment transaction with the Australian public. In Sydney, the Governor commented on the RBA survey finding that identified this trend:

What we discovered was that the [payment method] that was most expensive to the community was actually growing faster than the ones that were cheaper to the community...we published various research studies which concluded that the method by which the pricing was constructed and various prohibitions on merchant behaviour were the things that contributed to this.¹

1 *Official Hansard*, 4 June 2004, Sydney, p. 27.

- 3.3 In Brisbane, the RBA asserted that through reform it is endeavouring to make the true cost of credit cards visible to customers. By reducing credit card interchange fees, the banks are being forced to increase direct charges to credit card holders. The Governor contended that this move was necessary to bring credit cards more into line with other payment systems.²
- 3.4 The RBA informed the Committee of its progress in the reform of credit cards. The Governor noted that, as mentioned at the Brisbane hearing, the legal challenges brought against the RBA's reforms to credit card schemes by MasterCard and Visa were dismissed by the Federal Court. Moreover, whilst both schemes appealed, Visa has subsequently decided to cease its action.
- 3.5 The new interchange fees for Bankcard, MasterCard and Visa which came into effect at the end of October 2003 have achieved almost a 50 percent reduction in interchange fees. The RBA continues to monitor the flow-on of these savings to merchant service fees and at the June hearing Mr Macfarlane noted that:
- The reduction in the interchange fee has been carried through to the merchant service fee, which means that the banks are now receiving about \$430 million a year less than they formerly were in fees from the merchants for credit cards.³
- 3.6 In response to questions from the Committee about the banks' 38 percent increase in credit card fee income⁴, the Governor responded that the RBA is not overly concerned with banks charging fees:
- We do not object to bank fees. We thought the movement away from a situation where banks got all their income from the interest rate margin to one where they have a narrower interest rate but charge a fee for service was not only an improvement but also something that had to happen...We think that user pays, if it is done properly, is an acceptable system—particularly if there is a little safety net at the bottom, which there is.⁵
- 3.7 Mr Macfarlane added that in the RBA's view bank fees had not gone up disproportionate to the aggregate rise in banks' balance sheets. He said:

2 *Official Hansard*, 8 December 2003, Brisbane, p.24.

3 *Official Hansard*, 4 June 2004, Sydney, p. 27.

4 Reserve Bank of Australia, *Bulletin*, May 2004, p.58.

5 *Official Hansard*, 4 June 2004, Sydney, p. 26.

We do not subscribe to the view that [banks] have replaced the income lost through the narrowing of the spread by raising fees faster in a special attempt to regain that income. There are a lot of particular things we can say about bank fees, some of which we can approve of and some of which we can disapprove of, but I think that at the aggregate level they are just something the market has delivered...⁶

EFTPOS interchange fees

3.8 In the EFTPOS system in Australia there is a fee which the issuing bank pays to the merchant's bank, an EFTPOS interchange fee. This fee makes the issuing of EFTPOS cards costly for banks and encourages banks to recoup the cost through the imposition of fees on the cardholder.

3.9 The RBA's position is that EFTPOS interchange fees are 'totally unnecessary'⁷ and should not exist. At the Sydney hearing the Governor noted that in countries where EFTPOS works most efficiently such as Canada and the Netherlands there is no interchange fee. Mr Macfarlane further explained this position:

We talked to various people, including the banks and they eventually agreed to try and reduce it to zero. I want to mention that there is nothing in it for the banks because half the banks receive it and half of them pay it. For the banks, it was a zero sum game.⁸

3.10 Any change to the interchange fee involved authorisation from the ACCC because the initial setting of the fee had involved a collective action, as would agreement to set it at zero. In spite of the ACCC agreement to the change, the Australian Competition Tribunal disallowed the change on appeal, on the basis that the ACCC had not made a strong enough case that reducing the interchange fee was in the public interest.

3.11 The RBA noted that although it had opposed the appeal and remained in favour of the interchange fee being set at zero, it would now be considering what action to take in the future:

6 *Official Hansard*, 4 June 2004, Sydney, p. 26.

7 *Official Hansard*, 4 June 2004, Sydney, p. 28.

8 *Official Hansard*, 4 June 2004, Sydney, p. 28.

We believe that the majority of participants in the payment system would be in favour of having no interchange fee but we are not going to just go ahead and ignore the Competition Tribunal. We regard this as a new piece of information and we will consult again with the public. If we consult again, do further analysis and feel that there is a case for designation, we may well designate, which would bring it back into our court.⁹

- 3.12 The appeal was taken to the Australian Competition Tribunal by large retailers and oil companies, a group that would stand to lose significant income arising from their involvement in the EFTPOS network. The RBA's position however, is that this group are already gaining from the changes in credit card fees, particularly the capacity to 'surcharge'¹⁰ credit card costs and that lack of change to EFTPOS interchange means they are effectively getting a double bite at transaction fees income. A recent news article described the position of the RBA and other banks:

...the banks have argued retailers are seeking to protect the revenues from EFTPOS while also benefiting from credit card fee cuts of more than \$400 million annually.¹¹

- 3.13 The Committee expects an update from the RBA at the next hearing.

ATM fees

- 3.14 Currently, someone wishing to utilize a foreign ATM – that is, an ATM not owned by their bank or financial institution - is charged a foreign ATM fee. Most customers are unaware as to what this fee is until after the transaction has taken place, usually when they receive a statement.¹²
- 3.15 The RBA indicated that the industry steering group that is addressing ATM reform is proposing the elimination of the current ATM interchange fee (underpinning the average foreign ATM fee) and

9 *Official Hansard*, 4 June 2004, Sydney, p. 29.

10 At the Sydney hearing, Mr Macfarlane noted that the term 'surcharge' is not technically correct but actually refers to the passing on of the banks' costs to the consumer at the point of purchase. The RBA credit card reforms allowed retailers the capacity for this passing on of costs.

11 Moullakis, J 2004, 'Don't bank on card reforms', *Australian Financial Review*, 22 July, p.60

12 *Official Hansard*, 8 December 2003, Brisbane, p.29.

moving in the direction of full disclosure of costs to consumers. The Governor expanded on this point:

[the] steering group, which consists of the banks, building societies and...the people who provide ATMS...are proposing to get rid of the interchange fee—again, getting rid of the hidden fee. They are proposing to replace it with an upfront fee, which you will see when you go to an ATM. If it is your own bank's ATM, maybe you will get it for nothing. But if you go to another ATM, which increasingly you will, there will be a fee up there and you will know how much it is going to cost you.¹³

3.16 The stated aim of this reform is to achieve greater transparency and competition in relation to ATM fees. It may lead to ATM owners using signs on their machines to set out foreign ATM costs to customers. Individuals would then have the necessary information to decide whether or not to make a transaction on a particular machine.

3.17 At the Sydney hearing the RBA expressed a strong view that foreign ATM costs are too high and that reform should address this:

I wish there was no distinction [between foreign and non-foreign ATM fees]. I have said to people that foreign fees are too high. They say: 'you do not have to use them. Just use your own bank's ATM'...I think you have to assume that the average person will use whatever is the most convenient ATM and that means most of the time it will not be the ATM provided by their bank.¹⁴

3.18 The Committee also questioned the RBA about the UK experience with ATMs and the relevance for that experience here in Australia.

3.19 The Governor described the UK ATM system as having two distinct parts. About 25 percent of the market is held by 'independent deployers' who are not deposit-takers. They have a single focus of the provision of ATMS and charge a fee for use of their ATMS. Banks are responsible for the remainder of the market share and the Governor noted that banks in the UK have come to a collective arrangement regarding fees:

13 *Official Hansard*, 4 June 2004, Sydney, p. 35.

14 *Official Hansard*, 4 June 2004, Sydney, p. 35.

In the UK banks have adopted a 'knock for knock' approach towards their customers. The major banks agreed not to charge any foreign user a fee for using an ATM.¹⁵

- 3.20 In Australia ATMs provided by third party providers have grown from none to about 25 percent in the last five or six years.¹⁶ The RBA noted that it did not see the growth in this area as a bad thing. In fact, Mr Macfarlane commented that it would provide ATM services where there currently were none:

I think the non-bank provider will charge what they can. And I do not think that is a particularly bad thing. At the moment there are a lot of locations where no-one would put an ATM because the volume is too low. It may well be that, in those locations that currently do not have an ATM, a non-bank provider might put an ATM in there at a higher fee than in a popular area.¹⁷

- 3.21 Although the RBA believes that non-bank providers will charge what they can, it did not believe that reforms to the ATM system would encourage banks to pursue a differential scale of fee charging, for example, charging rural and regional users at a higher cost:

...at the moment banks do not charge a different fee for any of the services they provide to rural customers compared to city customers...I would expect that to continue if banks were free to charge whatever they wanted on their ATMs. I would expect they would be mad not to—the reaction would be so overwhelming...I think they would continue with their current practice of charging the same amount, wherever you came from.¹⁸

- 3.22 The Committee, however, is aware of at least one regional bank that is considering differential fee charging.¹⁹

- 3.23 The Committee is of the view that an overall review of the payments system may be beneficial to the implementation of reforms. Given the likely timing of the Federal election, this is a matter for the Committee to pursue in the next Parliament.

15 *Official Hansard*, 4 June 2004, Sydney, p. 35.

16 *Official Hansard*, 4 June 2004, Sydney, p.36.

17 *Official Hansard*, 4 June 2004, Sydney, p. 36.

18 *Official Hansard*, 4 June 2004, Sydney, p. 35.

19 Bank of Queensland Limited, *Submission to RBA: ATM system designation*, 8 July 2004, Brisbane, p.2.

RBA Governance

Activities of RBA board members

3.24 The Committee questioned the Governor on issues of conflict of interest among board members following publication of a news item stating that the Governor had prevented a board member from taking an 'outside advisory role with a property investment fund'.²⁰

3.25 The Governor explained that the bank had specific policies on such matters. He went on to say:

The article you refer to was not so much about advising but receiving an income and share options for involvement in what I regarded as a form of financial intermediary. In my view, there would be a conflict of interest in that case so that activity did not go ahead.²¹

3.26 Mr Macfarlane went on to note that while the *Reserve Bank Act 1959* had always prohibited board members from being directors or employees of banks and had widened that to any deposit-taking institution, he felt there was scope to go further:

But in my view that is not wide enough. I think it should be any supplier of finance. If you are an employee or a director of a supplier of finance, which means some form of financial intermediary, I think there is a conflict between that and sitting on the Reserve Bank board, where we spend so much of our time trying to limit the amount of finance that is going out. That was the basis of [my] decision.²²

3.27 The Committee is inclined towards effective polices that deal with governance issues for the RBA.

20 Garnaut, J. 2004, 'Central bank mandarins in tangle over outside interests', *Sydney Morning Herald*, 31 May

21 *Official Hansard*, 4 June 2004, Sydney, p. 38.

22 *Official Hansard*, 4 June 2004, Sydney, p. 38.

Recommendation 3

That the Government consider amendments to the Reserve Bank Act to extend the restrictions applying to the activities of board members to include all suppliers of finance, irrespective of whether the supplier is considered to be an authorised deposit taking institution.

Conclusion

- 3.28 The public hearing in Sydney again demonstrated the value of the Committee's biannual hearings with the RBA. The hearing was well-attended by the public, student groups and others, and as always attracted considerable interest from financial markets and the media.
- 3.29 The Committee thanks the RBA for its support for the hearings conducted during this Parliament, and looks forward to continuing this productive process following the pending Federal election.

David Hawker MP
Committee Chairman

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