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## GENERAL COMMENT ON REFORM OF THE AUSTRALIAN PAYMENTS SYSTEM

5 May 2006

The Australian Consumers' Association (ACA) welcomes the opportunity to comment on the on-going reform of the payments system to the House of Representatives Standing Committee on Economics, Finance and Public Administration.

ACA is an independent not-for-profit, non-party-political organisation established to provide consumers with information and advice on goods and services, health and personal finances, and to help maintain and enhance the quality of life for consumers. ACA publishes independent and expert consumer advice, conducts research into consumer issues including surveys into consumer attitudes, and advocates for improved conditions for consumers

ACA is uniquely positioned to comment on reform of the payments system. We do not stand to gain or lose financially from any of the reform proposals. We are motivated to comment because we believe that Australian consumers deserve a transparent, efficient, and lower cost payments system.

We have commented on numerous stages of the RBA reform process. The following table summaries our position on each step of the reforms. ACA generally believes the RBA reforms process is making the payments system relatively more efficient and transparent. However, we believe there are some barriers to effective reform. In particular more could be done to assist demand-side competition in the reform process. It is here the RBA's regulatory 'tool kit' needs further consideration.

<i>Reform</i>	<i>ACA Response</i>
Standard interchange fee on Visa and Mastercard Credit Cards	Supported, but with qualification on the form the interchange fee standard <sup>1</sup>
Allowing non banks to issue credit cards	Supported <sup>2</sup>
Removing the 'no surcharge rule' on Visa and Mastercard	Supported, but based on UK experience we argued that surcharging model failed to account for market power issues.
Decision not to designate ATM interchange fees	Disappointment at the decision not to designate ATM interchange fees. ACA remains opposed to a direct charging

<sup>1</sup> ACA Submission 15/3/2002

<sup>2</sup> ACA Submission 15/3/2002

	model. We are concern direct charging will disproportionately impact on consumers forced to use lower volume ATMs particularly in rural and regional areas <sup>3</sup>
Abolish 'honour all cards rule'	Concern that this reform might create a competitive disadvantage for institutions using VISA debit <sup>4</sup>
Adoption of a cap and floor on EFTPOS interchange fees	Broadly support <sup>5</sup>
Adoption of a cap on the weighted-average interchange fee on the VISA debit system	Broadly support <sup>6</sup>
Rules on bilateral behaviour in the EFTPOS system	Broadly support <sup>7</sup>

These issues are discussed in detail in a discussion paper prepared for ACA by Dr. Sacha Vidler of the University of Western Sydney. We make this report available to the committee as part of our submission. It assesses the strengths and weaknesses of the RBA reform program from a consumer perspective. To summarise, ACA is concerned that the current approach may not produce the optimal outcomes the RBA hopes for due to unrealistic assumptions about the reaction by consumers and other market participants to transparency and interchange reforms.

The market for consumer payment services is complex. The idea that consumers could, if presented with discrete transaction costs, weigh up the costs and benefits of each payment mechanism in such a way that competitive pressure might influence the delivery of those services is unlikely. To make efficient choices at the margin, consumers would need to be abreast of a number of payment mechanisms characteristics and their own precise financial status, including knowing various account balances, numbers of transactions executed per month, and the value of loyalty program benefits and interest free periods. As behavioural economics clearly demonstrates, the assumption that consumers will use information optimally, in an economic sense, is wrong in a wide variety of non-trivial ways. This is evident in the fact that volume of consumer withdrawals from foreign-ATMs recently became greater than the withdrawals from own-bank ATMs.

There are also policy measures that need to be in place that improve demand-side competition in the payments system. Because transaction accounts offered by financial institutions provide the 'consumer interface' to the payments system, some attention needs to be given to overcoming

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<sup>3</sup> ACA Submission 13/7/2001

<sup>4</sup> ACA submission 28/4/2005

<sup>5</sup> ACA submission 17/02/2006

<sup>6</sup> ACA submission 17/02/2006

<sup>7</sup> ACA submission 17/02/2006

<sup>8</sup> A system where consumers can authorise their new bank to get details of their direct debits and standing orders from their old bank. As they receive confirmation that each payment has been switched, the new bank will cancel the obsolete payments at the old bank

consumer inertia in changing banks. The adoption of UK Switching Mandate form might be one such step the committee could consider<sup>8</sup>.

The second barrier concerns the limited substitutability of various payments mechanisms. This refers to those situations for which only one payment mechanism is available. Limited substitutability undermines direct competition and requires consumers to use specific payment mechanism under particular circumstances. By way of example, ACA considered an essential aspect of the reforms associated with EFTPOS would be encouraging its development as a 'card not present' transaction system prior to, or contemporaneously with, designating EFTPOS and debit card interchange fees.

In summary:

1. ACA supports the general direction of the payment system reforms undertaken by the RBA.
2. The RBA may require additional powers to complete the task.
3. So long as there remains no viable non credit alternative for phone and internet transactions, ACA does not support measures that shift consumers from debit card to credit card products.
4. Policy measures should focus on improving demand-side competition and having close regard to barriers that include transaction costs and real world consumer behaviour.
5. Increasing substitutability of rival payments systems, particularly through an improved EFTPOS system, should be a priority of payments reforms.

We would be happy to discuss these issues further with the committee.

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