

The applications

- 3.1 On 21 February 2003 applications A30224 and A30225 were lodged with the Commission seeking authorisation of an Interchange Fee Agreement (the proposed Agreement). A copy of the proposed Agreement is attached to this determination (**Attachment A**). The proposed Agreement broadly provides for the collective setting of EFTPOS interchange fees to zero.
- 3.2 Application A30224 was lodged under sub-section 88(1) to make and give effect to a contract, arrangement or understanding, which contains a provision which is, or may be, an exclusionary provision within the meaning of section 45 of the Act.
- 3.3 Application A30225 was lodged under sub-section 88(1) to make and give effect to a contract, arrangement or understanding, which has the purpose or effect of substantially lessening competition within the meaning of section 45 of the Act.
- 3.4 The Applicants have also requested that, pursuant to s 88 (10) of the Act, in granting authorisation to the proposed Agreement, the Commission also grant authorisation providing immunity to persons who may become parties to the proposed Agreement after it has been made and the giving effect to it authorised.

The Interchange Fee Agreement

Setting of EFTPOS interchange fees

- 3.5 Clause 2.1 of the Agreement provides that the Applicants agree to charge and to receive the following interchange fees for any EFTPOS transaction in Australia in which at least one of the parties is an EFTPOS issuer or EFTPOS acquirer:

Transaction Type	EFTPOS Interchange Fee (cents)
(a) EFTPOS Withdrawal Transaction (including sales, sales/cash-out and cash-out only)	Zero
(b) EFTPOS Declined Transaction	Zero
(c) EFTPOS Reversal Transaction	Zero

Inconsistency with contractual obligations

- 3.6 Clause 2.2 (a) of the proposed Agreement provides that each party to the Agreement agrees that any provision of an existing contract, to which the only parties are any two or more of the parties to the proposed Agreement, and which sets an interchange fee for EFTPOS Transactions in Australia at any level other

than set out in clause 2.1, is hereby amended so that the EFTPOS interchange fee between parties to this Agreement is governed by clause 2.1.

- 3.7 Clause 2.2 (b) of the Agreement provides that if clause 2.1 of this Agreement is inconsistent with a provision of any existing contract, the parties to which include one or more parties to this Agreement and one or more parties who are not parties to this Agreement, those parties to this Agreement who are also parties to the existing inconsistent contract will use their reasonable endeavours to amend that contract as soon as practicable to remove the inconsistency.
- 3.8 The Commission notes that while the proposed Agreement does not make specific provision for non-existing (or new) contracts, it is understood from the Applicants' submission that it is intended that the zero interchange fee will apply to bilateral arrangements entered into between incumbents and potential new entrants.¹³

Review and monitoring

- 3.9 Clause 3.1 of the Agreement provides that the parties agree that they will monitor EFTPOS interchange fees and the impact of the changes on an on-going basis and meet at least annually.
- 3.10 Clause 3.2 provides that the parties to the Agreement will conduct a review of the EFTPOS interchange fees set out in clause 2.1;
- (a) every 3 years (approximately) from the date of commencement (unless a review under (b) has been conducted within the prior 2 years); and
 - (b) at any time, if there is a material change in circumstances and at least 25% of the parties in number request such a review.
- 3.11 Clause 3.3 provides that the Agreement may be amended pursuant to a review under clause 3.2, if no less than 75% of the parties in number agree to the amendment. Where such an amendment is not agreed to unanimously, the amendment will not come into force for at least 120 days.

¹³ For example Applicants submission, February 2003, at page 23.

Submissions prior to the draft determination

The Applicants

- 4.1 Prior to the Commission's draft determination, the Applicants provided two written submissions in relation to the applications for authorisation, being a lodgement submission (February 2003) and a rejoinder submission provided in response to public submissions by interested parties (April 2003). Commission staff also met with representatives of the Applicants for an oral briefing (29 April 2003). Copies of the non-confidential submissions provided by the Applicants are kept on the Commission's public register. Provided below is a brief summary of the Applicants' submissions in terms of public benefit and effect on competition. The Applicants' submissions are considered in more detail in chapter 6 of this determination.
- 4.2 The Applicants advise that the applications result from the review of interchange fees by the RBA and the Commission and the subsequent deliberations of the EIWG. The primary purpose of the proposed arrangement is to make EFTPOS more attractive to cardholders (particularly relative to credit cards) than it is at present and hence to address concerns about efficiency in the payments system. The Applicants submit that the concurrent proposed amendments to credit card interchange fees (outlined at paragraphs 2.23 to 2.27) will assist, but the proposed EFTPOS change will still be beneficial in addressing the problem.

Market definition

- 4.3 The Applicants submitted that the proposed conduct will have a direct effect in the market for retail banking and that there will be an indirect effect on the market for retail goods and services. In providing these market definitions, the Applicants noted that in their view there is no useful market definition that would bring these markets under one umbrella and that furthermore there is no useful reason to seek one. It is the Applicants' view that the essence of analysing competitive impacts of potentially anti-competitive conduct is to examine all relevant markets and not to assume that one is paramount or that all the effects of the conduct are in one market.
- 4.4 The Applicants submitted that, whilst the market for retail banking may be oligopolistic in structure (exhibiting a high degree of market concentration), inter-firm rivalry occurring in a market place governed by principles of appropriate trade practices has led to the achievement of the desirable outcomes of a perfectly competitive market, such as a wide variety of products and strong innovation. It is the Applicants' view that, while the market for retail banking is not perfectly competitive, it is nonetheless 'effectively competitive'.

Public benefits

- 4.5 The Applicants claim that the proposed arrangement will be likely to result in a number of public benefits, including:

- making EFTPOS more attractive to consumers relative to less efficient means of payment, thereby inducing a shift towards the use of EFTPOS and reducing the overall cost of the Australian payments system;
- introducing greater flexibility into the setting of EFTPOS interchange fees; and
- making entry as a new issuer or acquirer of EFTPOS transactions easier by simplifying the negotiation of bilateral interchange agreements.

Making EFTPOS more attractive

- 4.6 The Applicants submitted that the proposed conduct will result in a reduction of the costs incurred by card issuers in providing debit card services to cardholders. It is the Applicants' view that effective competition between issuers in the retail banking market is likely to lead to those cost reductions being passed on to cardholders through lower banking fees and/or enhanced services.
- 4.7 Acquirers are likely to increase merchant service charges so as to replace the income stream previously provided by interchange fees. The Applicants claim that effective competition in retailing is likely to see merchants recover their higher costs through a general (although inconsequential) rise in the price of goods and services, rather than through surcharges for the use of EFTPOS.
- 4.8 Therefore the proposed conduct will mean that consumers face a lower relative cost of using EFTPOS compared with other means of payment. This is likely to lead to substitution by consumers towards the use of debit cards and away from credit cards in their payments for goods and services. The Applicants claim that, as argued by the RBA, this will give rise to public benefits through improvements in the efficiency of the payments system as a whole.
- 4.9 In response to concerns by interested parties about the pass through of interchange reforms, the Applicants agree that commercially appropriate disclosure (in addition to the current regulatory imposed disclosure regimes) and information campaigns may be useful and appropriate to help smooth the adjustment to new levels of cardholder fees and merchant service charges.
- 4.10 However, in relation to the pass through of savings to cardholders and the price signals consumers are likely to face, the Applicants claim that the change in interchange fees will not always necessarily be passed through in an easily observable manner. The Applicants advise that they anticipate the reduced costs to be passed on in some form – such as lower retail banking fees and/or through enhanced services and/or higher transaction account deposit interest rates. However, given the fee and charge structures of financial institutions it is unlikely that such a change would be in the form of a simple pass through of 'X' cents per transaction.

More flexible interchange fees

- 4.11 The Applicants advise that the current arrangements whereby interchange fees are set as part of the bilateral agreements create a difficulty in renegotiating agreements and creates an inertia that discourages any review and change in interchange fees despite changes in market circumstances.
- 4.12 The Applicants claim that under the proposed Agreement the level of the interchange fee will be reviewed after three years, or earlier, which will introduce greater flexibility into the fee level.

Assist new entry as an issuer or acquirer

- 4.13 It is the Applicants' view that the proposed Agreement will make entry as a new card issuer or merchant acquirer of EFTPOS transactions easier by simplifying the negotiation of bilateral interchange agreements. In particular, the Applicants submitted that the proposed conduct would ameliorate the extent of natural barriers to direct entry into the EFTPOS market by making bilateral negotiations between parties easier through the removal of one element of negotiation – interchange fees.
- 4.14 In any event, the Applicants claim that access issues are more appropriately handled by the APCA in the context of a review of the authorisation of the CECS arrangements. The Applicants advise that the APCA has already commenced a detailed examination of access and related issues.

Anti-competitive detriments

- 4.15 The Applicants submitted that in assessing the anti-competitive detriment arising from the proposed Agreement it is important to distinguish the effect of the proposed conduct from the effect of the existing CECS arrangements. It is the Applicants' view that the proposed conduct will not have any adverse effect on natural barriers to entry facing potential card issuers or merchant acquirers and that there is no reason to expect that the proposed conduct would result in the withdrawal of existing market participants nor any lessening of competition between them.
- 4.16 It is the Applicants' view that, as the proposed Agreement provides that the Applicants will use their reasonable endeavours to negotiate zero interchange fees with new entrants, this will have the effect of eliminating any market power that an existing card issuer or merchant acquirer might otherwise have been able to exercise in respect of negotiations involving the level of the interchange fee.
- 4.17 In addition, it is the Applicants' view that, although potential new merchant acquirers would not, as a result of the proposed Agreement, receive the prospective revenue stream from interchange fees as was available to existing merchant acquirers when they entered the market, new entrants would nonetheless be on the same footing as existing merchant acquirers when negotiating service fees with merchants.

- 4.18 The Applicants submitted that potential new entrants with efficient costs would suffer no detriment as a result of the conduct. In particular it is the Applicants' view that, although new entrants would necessarily be exposed to the realities of economies of scale and competitors whose costs were already sunk, these factors would have no effect on the setting of interchange fees.
- 4.19 The Applicants also claim that nothing in the proposed conduct will change the bargaining power of financial institutions vis-à-vis retailers. Effective competition in commercial banking will not only limit aggregate increases in merchant service charges to the loss of interchange revenue, but also ensure that there is no unwarranted redistribution of the costs of acquiring between classes of merchants in the process.
- 4.20 The Applicants have stressed that the proposed conduct is part of a package of payments system reforms. Merchants will now be significant direct beneficiaries of debit and credit card reform, taken together, in terms of the net cost incurred in accepting debit and credit cards. Merchants will also see their costs reduced over time as a result of changes to price signals that provide consumers with greater incentives to use lower cost payment methods.

Submissions by interested parties

- 4.21 The Commission initially sought submissions from a wide range of interested parties in relation to the applications for authorisation and received 34 public submissions. A copy of each submission is held on the Commission's public register. A list of interested parties who lodged public submissions is at **Attachment B**.
- 4.22 A summary of the main issues raised by interested parties, both in support and in opposition to the proposed arrangements, is provided below.¹⁴

Consumer organisations

- 4.23 Submissions were received from the following organisations that represent the interests of consumers – Aboriginal Co-ordinating Council (ACC), Australian Consumers Association (ACA), Consumer Credit Legal Service (WA) Inc (CCLS(WA)), Consumers Federation of Australia (CFA) and Consumer Law Centre of Victoria (CLC(V)).
- 4.24 In general terms the consumer organisations broadly support the proposed Agreement to the extent that the reduction of the EFTPOS interchange fee will

¹⁴ Responses, but no substantive submissions, were also received from the NSW Department of Fair Trading, the ACT Chief Minister, the Commonwealth Treasury, Bankcard Association of Australia, and the Commissioner for Consumer Affairs (SA).

enhance transparency and efficiency and deliver clearer pricing signals than those currently received by consumers.

- 4.25 However, there is concern that without some form of compulsion the banks will fail to pass on the expected cost savings to cardholders. The ACA, CCLS(WA), CLC(V) and CFA propose that as a condition of authorisation the applicants undertake to pass on the net savings to EFTPOS customers. They also propose that a prices oversight body be established to monitor merchant pricing and the direct charging of consumers by merchants and report to the Commission and public on the impact of the EFTPOS interchange fee agreement. This ongoing monitoring should feed into a review at the end of the authorisation period to assess whether the costs to EFTPOS customers have fallen and the impact the reforms have had on the use of EFTPOS relative to other payments systems.
- 4.26 The CFA, ACC and CCLS(WA) were also particularly concerned to ensure that savings were passed through to rural and remote consumers who often missed out on the benefits from such reforms given the limitations of the banking services currently provided to them.

Merchants

- 4.27 Submissions were received from the following merchants and organisations representing merchants – Australian Institute of Petroleum (AIP), Australian Retailers' Association (ARA), Caltex Australia Petroleum Pty Ltd, Coles Myer Ltd, McDonald's Australia Limited, Motor Trades Association of Australia (MTAA), National Association of Retail Grocers of Australia (NARGA), Post Office Agents Association Limited (POAAL) and Woolworths Limited.¹⁵
- 4.28 In general, merchants oppose the applications for authorisation as they claim that the proposed Agreement will be detrimental to competition in the EFTPOS market and would result in a negative public benefit. Submissions by merchants focussed on the following issues as being reasons for their opposition:
- the Applicants have not provided any data or evidence to support their arguments or demonstrate the effects of a zero interchange;
 - the proposal does not address the issue of network access. Access is a critical part of delivering increased competition to the EFTPOS market thereby keeping the costs of the system down. A multilateral fee does not make it easier for new acquirers to enter the market;
 - there is no evidence to suggest that the reduction in costs experienced as a result of a zero interchange fee will increase debit card usage as a result of card issuer savings being passed on to cardholders. Given the level of competition between banks and the fact that many EFTPOS cardholders currently have their fees waived by card issuers, it is likely that card issuers

¹⁵ Responses were also received from Metcash and Queensland Retail Traders & Shopkeepers Association indicating their views were included in other submissions.

will retain a substantial majority of the savings they make from the move to zero interchange;

- merchant principal investment in the EFTPOS network is significant and the current interchange fee arrangement enables merchant acquirers to reimburse merchant principals for their investments. This in turn ensures that the high standard and security of the EFTPOS network is maintained through future investment. The move to a zero interchange fee is likely to diminish the incentive for both merchant principals and merchant acquirers to invest in the ongoing development of the EFTPOS network;
- merchant acquirers will seek to recoup their loss in interchange fee revenue by increasing merchant service fees to retailers and service stations. Woolworths advises that merchants will be faced with an increase in their EFTPOS transaction processing costs of around 20 cents per transaction. merchants in turn will pass on the higher costs to consumers, most likely in the form of a general increase in prices. Thus all consumers will subsidise users of EFTPOS. McDonald's submits that a worst case scenario is that businesses may even choose to remove the EFTPOS facility;
- if all consumers pay for the cost of EFTPOS there is no transparency in pricing and correct pricing signals are not sent. This is the very problem the Joint Study identified as being significant in relation to credit and debit card reform; and
- there will not be an overall reduction in payments system costs, the result would simply shift costs away from card issuers to both consumers and merchants. This is an inequitable position as issuers derive the major benefit from the widespread adoption and use of EFTPOS. This does not represent effective reform.

4.29 NARGA and MTAA also submit that increases in merchant fees would impact disproportionately on small businesses. Under current arrangements, small retailers pay transaction fees and line rental charges, while large retailers such as supermarket chains and oil companies receive fees from merchant acquirers or are able to negotiate merchant fee reductions or other offsets by virtue of their market power. The net result is that a small retailer pays a higher cost per transaction, compared with a large retailer. Competition faced by small retailers means that they are often unable to pass on these costs to consumers and as such are forced to absorb them. Such a disadvantage is likely to be exacerbated under the proposed new arrangements.

4.30 The POAAL expressed concern for the unknown and unexpected consequences that may arise should the financial institutions attempt to recover the revenue from existing fees through other fees and charges, which in turn may be unrelated to the cost of providing such a service.

4.31 Caltex claims that the applicants rely almost exclusively on the Joint Study. However, Caltex submits that the Joint Study does not provide any basis upon which the Commission could be satisfied that the public benefits of a price fixing agreement in relation to debit card interchange fees outweigh the public

detriment of such an arrangement. Further, Caltex submits that there are a number of defects with the Joint Study that caused incorrect findings.

- 4.32 The AIP submits that if the Commission does authorise the application conditions should be imposed to ensure that future reviews of the EFTPOS arrangements are conducted independently of the banks; that card issuers be required to pass on all cost reductions or disclose enhanced services resulting from the arrangements to cardholders within a defined time period; merchant service charges by merchant acquirers should not change as a result of the arrangements and merchant acquirers should be required to enter into good faith negotiations with merchant principals, who have invested in EFTPOS infrastructure, to ensure that arrangements fairly reflect merchant investments; and access arrangements should be reviewed as part of this application to target maximum access at both issuing and acquiring levels.

Industry regulators

Reserve Bank of Australia (RBA)

- 4.33 The RBA agrees that the proposal will have significant public benefits, particularly as the lowering of transaction fees for debit cardholders will produce a more efficient set of price signals for consumers choosing between EFTPOS and other means of payment. Public benefits will be maximised if the reduction in interchange fees is passed immediately and in full to debit cardholders. The RBA advises that it can see no reason why debit card issuers, in a competitive market environment, should not do so.
- 4.34 The RBA advises that merchant acquirers can be expected to seek to recoup the loss of interchange fee revenue directly from merchants through increases in merchant service fees on EFTPOS transactions. The loss of EFTPOS interchange fee revenue received by merchant acquirers will be approximately \$150 million per year. The RBA submits that the extent to which the amount is recouped from merchants should be set against the reduction in merchant service fees from the reforms to credit card schemes which are expected to reduce credit card interchange fee amounts paid by acquirers by around \$350 million per year.
- 4.35 Merchants will therefore be significant beneficiaries of debit and credit card reform taken together, although the impact will differ across merchants depending on the mix of payment cards they accept. The RBA submits that merchants will also see their costs reduced over time as a result of changes to price signals that provide consumers with greater incentive to use lower cost payment methods. Competition will ensure that the lower costs incurred by merchants will pass through to consumers in the general level of prices.
- 4.36 While the RBA recognises that some large retailers have made significant investments in their own EFTPOS terminals and related infrastructure and have negotiated arrangements to share interchange fee revenue with their merchant acquirer as a means of recovering costs, there is no evidence that it is necessary for merchants to continue to recoup the costs of their initial investments or

upgrades. The RBA claims that if EFTPOS fee revenues are eliminated investment decisions by merchants would be determined by normal market mechanisms and merchants would continue to invest in EFTPOS facilities if there are direct benefits in doing so.

- 4.37 The RBA advises that reform also needs to address the issue of access to the EFTPOS network. The current bilateral arrangements are not beneficial to the Australian payments system and can be a significant barrier to new entrants. The elimination of bilateral interchange fees should facilitate access of new entrants to the EFTPOS network since they will no longer need to negotiate interchange fees as a condition of entry. Although without interchange fee revenues some incumbents may have less financial incentive to establish interchange links with potential new entrants.
- 4.38 The RBA supports the Applicants' suggestion that access issues are more appropriately dealt with in the context of reauthorisation of the CECS rather than the current applications. However the RBA advises that it would want to be assured that the APCA will address impediments to access to the EFTPOS network in a timely manner. A new entrant that is approved as a member of the CECS and meets the APCA's technical requirements should be entitled to exchange EFTPOS transactions with any other CECS member in a timely manner and at reasonable cost. The RBA submits that over the longer term the industry might want to consider the case for developing an industry owned switch to facilitate access and encourage competition and efficiency in the operation of the EFTPOS network.

Australian Securities and Investments Commission (ASIC)

- 4.39 The ASIC recognised the potential for the proposal to result in real savings for consumers and to encourage consumers to use lower cost payment mechanisms. The ASIC advised that this potential is, however, dependent upon consumers receiving the benefit of the reforms in terms of significantly reduced EFTPOS banking fees.
- 4.40 The ASIC submitted that as the proposal has no built in mechanism to ensure that fee reductions are passed on to consumers it would be sensible for authorisation to bolster the chances of this happening. For example, by making it clear that any renewal of the authorisation would be dependent upon proof that the reduction of interchange fees to zero had resulted in a significant reduction in the fees consumers' financial institutions charged them for their part in processing EFTPOS transactions.
- 4.41 In addition, the ASIC has submitted that it is essential that there is adequate disclosure about the new system. In particular, it should be a requirement that all merchants who surcharge for EFTPOS transaction disclose the amount of the surcharge prior to the transaction. The ASIC also propose that it should be a requirement that all parties to the EFTPOS agreement provide cardholders with a clear explanation of the rationale of the reforms and the implications for the fees payable by cardholders, including disclosure of whether or not the standard fees for EFTPOS transactions are reduced and by how much.

- 4.42 On a related point, the ASIC raised the issue about whether a cap should be placed on merchant surcharging as there is anecdotal evidence that in rural and remote areas, where there is little competition, merchants had imposed extremely high EFTPOS surcharges that would seem to far exceed the cost to the merchant of providing the service.

Government Ministers

Minister for Tourism and Racing and Minister for Fair Trading – Queensland Government – The Hon. Merri Rose MP

- 4.43 The Minister provided in principle support to the proposal which is likely to lead to cost reductions being passed on to consumers. However, the Minister noted that a review of the fee structure in three years or earlier should determine whether the assumptions upon which the proposal are based have in fact eventuated and therefore a more informed decision could be made on the merits of any future proposals.

Minister for Consumer Affairs – South Australian Government – The Hon. Michael Atkinson MP

- 4.44 The Minister was of the view that the proposed Agreement will benefit consumers:
- through a decrease in transaction fees for transaction accounts;
 - by making EFTPOS a cheaper form of payment than credit cards (coupled with credit card reforms);
 - by making fees more transparent and flexible so that they remain at levels sufficient only to recover costs with savings passed on to consumers; and
 - if, as a result of the fee level being multilaterally set, negotiations of agreements with new entrants are less complicated, new entry will be easier and therefore competition will increase with flow on pricing benefits to consumers.
- 4.45 The Minister noted that these benefits would rely, to some extent, on financial institutions not seeking to recoup lost revenue from interchange fees by increasing direct fees to cardholders and merchants. It is therefore important that regulators strictly monitor the carrying out of the agreements to ensure the desired effects identified in the Joint Study are realised.
- 4.46 The Minister also noted that, given the conclusion of the Joint Study, a better option would be eliminating fees altogether. Although the proposed Agreement is a compromise that appears to deliver the major benefits of elimination for at least the life of the Agreement.

Minister for Regional Development, the Illawarra, and for Small Business – New South Wales Government – The Hon. David Campbell MP

4.47 The Minister submitted that the Applicants had not made a sufficient case in support of a zero interchange fee and expressed concern that the economic interests of stakeholders may be a barrier to them jointly reaching agreement on a position in relation to debit card interchange fees. In particular the Minister submitted that:

- there should be an extension of the timeframe of the debit card/EFTPOS review;
- a review panel should be established by the RBA comprising representation of all stakeholders, including consumers and small businesses, and facilitated by the RBA; and
- the scope of the review should be expanded to include all debit card schemes and related fees.

Others

Australian Bankers' Association (ABA)

4.48 The ABA advises that it supports the application as setting the EFTPOS interchange fee to zero will provide greater incentive for people to purchase goods and services using their debit card relative to credit cards. This will provide greater economic efficiency consistent with the RBA's claims that debit cards are a more efficient form of payment than credit cards.

4.49 The ABA claims that merchants will benefit from the package of debit and credit card reforms and that EFTPOS and credit card reforms should be introduced concurrently to minimise any potential disadvantage. The ABA claims that large retailers have a strong financial incentive to oppose the concurrent introduction of EFTPOS and credit card reforms.

Australian eCommerce Network

4.50 The Australian eCommerce Network opposes the proposed EFTPOS fee reform as the proposal is self interested and ignores many of the most significant aspects of the current EFTPOS system, such as the fact that banks exercise an oligopolistic control over the system. All but the largest retailers and merchants have little option but to rent their EFTPOS terminals from the banks. So if the banks suffer any revenue reduction from the proposal, fees to merchants for their EFTPOS facilities will inevitably rise.

Cosmos E-C Commerce Pty Limited

4.51 Cosmos seeks the assurances of the RBA and Commission that new parties wishing to enter the EFTPOS acquiring market are protected from anti-competitive behaviour.

First Data Resources Australia Limited

- 4.52 First Data advised that it supports the proposed arrangements. First Data has provided third party processing services to the retail payments industry, including EFTPOS acquiring services for both merchants and financial institutions for the past 20 years.

Macquarie Corporate Telecommunications Pty Ltd

- 4.53 Macquarie submitted that there is currently a restriction on the telecommunications services over which EFTPOS services are provided. In the interests of competition in the telecommunications market and to reduce the cost of EFTPOS services, the Commission should include a requirement that carriers other than Telstra Retail are able to bundle EFTPOS solutions.

MasterCard International

- 4.54 MasterCard advises that it regards the EFTPOS system as being competitive with its credit card system in use in Australia.
- 4.55 MasterCard submits that the Applicants have not provided information as to how the zero rate of interchange fee proposed is arrived at. MasterCard believes there should be some methodology employed to ascertain the appropriate interchange fee rather than it being set on what appears to be an ad hoc basis. This is particularly given that interchange fees for credit card systems are now regulated by the RBA and to have a major competitor setting interchange fees in such a manner may lead to a perverse anti-competitive result. MasterCard considers that it is in the public interest that interchange fees for EFTPOS should be determined by reference to a transparent methodology.
- 4.56 Further, MasterCard believes that if there is no methodology used to ascertain the zero rate, how will the proposed review of interchange fees be undertaken and what criteria will the zero rate be compared against.
- 4.57 MasterCard submits that, consistent with the participants in the credit card system, the RBA and the APRA should consider the introduction of a regime providing for prudential regulation and supervision of all EFTPOS participants.
- 4.58 MasterCard also submits that it is more likely that merchants with market power will impose surcharges in respect of EFTPOS and credit card transactions as they are not subject to competitive pressures faced by other merchants. MasterCard regards it as objectionable that merchants with market power are able to extract surcharges from consumers in these circumstances.
- 4.59 MasterCard also outlined its disagreement to references made by the Applicants to the four-party credit card schemes and the RBA regulations. MasterCard's detailed views on the RBA's regulations are found in its submission to the RBA located at www.mastercard.com/au/rba/.

MoneySwitch Ltd

- 4.60 As a potential new provider of merchant acquiring services, MoneySwitch submitted that the proposed Agreement is likely to result in a significant cost disadvantage for new entrants, in particular as under a zero interchange fee card issuers will have no incentive to lower access costs by adopting appropriate technology and standards. Further it is MoneySwitch's view that the proposed Agreement does not address issues such as commercial, technical, operational, testing, communications and attachment costs, and that these will still have to be negotiated by incumbents and potential new entrants.
- 4.61 However, new entrant merchant acquirers must still negotiate other items (commercial, technical, operational, testing, communications and attachment costs) on a bilateral basis with all card issuers. MoneySwitch submits that as the card issuing organisations (banks) are also largely involved in merchant acquiring activities they have no incentive to assist new merchant acquirers because this will negatively impact on their own merchant acquiring business. This makes it very difficult for a new merchant acquirer to negotiate a fair and balanced agreement in a reasonable time frame.
- 4.62 MoneySwitch submits that gateway providers do not solve the problem because the fees charged by the gateway add a significant cost that major existing merchant acquirers do not have to bear. The cost disadvantage for the new entrant significantly lowers their business viability and reduces competition in the merchant acquiring marketplace.
- 4.63 MoneySwitch submits that it is essential that conditions be imposed to enable and encourage new entrant merchant acquirers, including requirements for existing issuers to:
- negotiate the interconnect agreement in the utmost good faith;
 - allow connection using modern networking technology; and
 - set attachment fees on a verifiable cost recovery basis, without overheads.

SingTel Optus Pty Limited

- 4.64 Optus advises that it is a major supplier of telecommunications services to the banking and finance sector including services used for the provision of EFTPOS. Optus supports the proposed Agreement as Optus considers that it will stimulate the use of EFTPOS as a means of payment and in turn increase the number of EFTPOS payments and their proportion of total payments.

Draft determination and pre-determination conference

- 5.1 Before determining an application for authorisation the Commission is required to prepare a draft determination stating whether or not it proposes to grant authorisation to the applications and summarising its reasons. The Commission released a draft determination proposing to deny authorisation to applications A30224 and A30225 on 8 August 2003.

Overview of draft determination

- 5.2 In its draft determination the Commission noted that it considers that reform of the EFTPOS network, including interchange fees, is necessary in order to encourage competition and efficiency in the operation of the network. The Commission considered that this will in turn contribute to the overall efficiency of Australia's payments system. The Commission noted that a package of reforms addressing access, interchange fees and pricing transparency in the credit card network had recently been implemented by the RBA and that these reforms are intended to encourage competition and efficiency. However in its draft determination the Commission expressed concern that the applications for authorisation addressed only one element of the necessary reform – that is to EFTPOS interchange fees.

Anti-competitive effect of the proposed Agreement

- 5.3 The Commission in its draft determination considered that there were several factors that were likely to influence the effectiveness of competition among card issuing institutions and merchant acquiring institutions, including the high degree of market concentration; the dominance of a small number of large institutions; the cross representation between card issuers and merchant acquirers; and the high barriers to entry to both card issuing and merchant acquiring. It was the Commission's view that, in such a market environment, the proposed interchange fee arrangement was likely to result in a lessening of competition. In particular it may increase the (already high) barriers to entry by removing an important negotiation incentive which may further entrench market concentration.
- 5.4 The Applicants submitted that such detriment could be offset to some extent by the potential liberalisation of access to the EFTPOS network as part of the APCA review of the CECS arrangements. However it was the Commission's concern that, in the circumstances, the outcome of the APCA review process was highly uncertain. As such it was the Commission's view that it would be inappropriate to attach a lesser weight to the likely anti-competitive detriment resulting from the proposed Agreement on the basis of the APCA review. The Commission however considered that, in the event that suitable access reform was to be introduced, the proposed Agreement was more likely to be in the net public benefit.

Public benefits

5.5 The Commission in its draft determination considered that the proposed Agreement has the potential to result in benefits to the public, in particular as the proposed Agreement may contribute to improved payment system efficiency. However in the circumstances presented the Commission was concerned that the weight to be attached to the potential benefits were uncertain. In particular the Commission was concerned that competition between card issuing institutions may not be sufficient to ensure a lasting pass through of the savings by card issuers to cardholders benefit enjoyed by the public and further that the current barriers to entry may inhibit the competitive pressures that may otherwise be exercised by potential new entrants (which would thereby increase the extent and likelihood of that benefit being passed through to the general community). The Commission was also concerned that transparent pricing signals that would encourage greater payments system efficiency may not be readily observable by consumers and that the proposed Agreement was unlikely to improve the flexibility of interchange fees (as it would continue to maintain standardised fees, albeit at zero). Consequently the Commission was of the view that the public benefits likely to flow from the proposed Agreement were uncertain were not sufficient to outweigh the detriment likely to flow from the proposed Agreement.

5.6 In the draft determination the Commission indicated that in its view a commitment to suitable access reform establishing an appropriate timeframe (or in the absence of such commitment, action by the RBA) could go some way to addressing the uncertainty associated with the interchange fee proposal. In order to facilitate industry discussion the Commission invited submissions addressing the EFTPOS access reform principles identified by the RBA and the prospects of a commitment to these principles in accordance with the RBA's proposed timetable.

Pre-determination conference

5.7 Pursuant to section 90A of the Act, the Applicants requested the Commission convene a pre-determination conference in relation to the draft determination. The conference was held in Canberra on 1 September 2003 and a record of the submissions made by the Applicants and interested parties at the conference is held on the Commission's public register.

5.8 Following the draft determination and the pre-decision conference the Commission also received a number of written submissions from the Applicants and interested parties. A list of parties who provided submissions, including at the pre-decision conference, is at **Attachment C**. A copy of non-confidential submissions is held on the Commission's public register.

Summary of submissions received following the draft determination (including at the pre-determination conference)

The Applicants

- 5.9 The Applicants submitted that the Commission in its draft determination understates the public benefits which are likely to result from the proposed conduct and overstates any lessening of competition likely to result from the proposed conduct. The Applicants further submit that there is clearly a net public benefit from the proposed conduct and that the Commission should grant authorisation. The Applicants submit that in particular, it is likely that cost savings generated by the proposal will be passed on in some form to card holders sufficiently to result in an overall public benefit.

Effect on competition

- 5.10 The Applicants consider that the Commission has implied that interchange fees are currently set in a normally competitive environment and that they are readily renegotiated. The Applicants consider that the Commission has ignored evidence regarding the considerable uniformity of interchange fees and the fact that they are unlikely to be altered.
- 5.11 The Applicants consider that the fact that interchange fees are currently not easily alterable does not detract from the substantial competitive forces at work to allocate the costs of the EFTPOS network between merchants and consumers.

Card issuing

- 5.12 The Applicants submit that there are a significant number of card issuing institutions and that the presence of smaller financial institutions ensures continued pricing innovation and operates as a significant competitive constraint on the four major banks. The Applicants note that RBA statistics show that the market share of players other than the four major banks is in fact larger than indicated by the figures relied on in the draft determination, and is growing. The Applicants submit that there is strong competition between card issuers as evidenced by the fact that many of the smaller institutions absorb the costs of the current interchange fees rather than charging explicit transactions fees and that there is variation in price / service / quality bundles provided to retail customers by the many card issuers. The Applicants consider that to refute the presumption of effective competition, evidence must be presented of at least tacit collusion between card issuers.

- 5.13 The Applicants acknowledge that there may be some barriers to entry into the market for card issuing that could be addressed by reforming the conditions for access to the EFTPOS network. The Applicants submit however that, for the purposes of this application for authorisation, the relevant issue is that the proposed conduct sought to be authorised does not increase barriers to entry. No argument has been made to suggest otherwise and potential card issuers have not provided information to suggest that they are concerned by the potential change to interchange fees.
- 5.14 The Applicants consider that the concern expressed in the draft determination that the proposed arrangement may have the effect of increasing barriers to entry and may act to further entrench the high level of card issuer concentration is based upon a purely theoretical and very partial discussion of the effect of one particular source of revenue for acquirers. Further the Applicants consider that concerns expressed in the draft determination about removing the interchange fee revenue stream making it more difficult for potential new entrant issuers to negotiate bilateral agreements ignore the central question as to whether the current revenue stream from interchange fees is appropriate.
- 5.15 The Applicants submit that the Joint Study establishes that interchange fees are not justified on a cost basis, i.e. having regard to the *cost per transaction* and that no 'recompense' in this form, from issuers to acquirers, is appropriate at all. The Applicants submit that, in any event, there is nothing in the proposed interchange fee arrangements to prevent potential card issuers from making a transfer to incumbent merchant acquirers so as to provide an incentive for them to accommodate new entry. The Applicants consider that such transfers could take many forms, and that the proposed conduct would only exclude them being set on a per transaction basis along the lines of interchange fees.
- 5.16 In a separate submission the Bank of Queensland (BofQ) submitted that it considers that the proposed Agreement would substantially 'level the playing field', enabling smaller institutions to compete more effectively in card issuing. In particular the BofQ notes that it does not consider that there are currently high barriers to entry as, to the best of its knowledge, all Australian financial institutions who issue debit cards have their cards accepted in the EFTPOS system. The BofQ notes that regulatory barriers (being those that must be satisfied in order to become an ADI) are not relevant to the proposed Agreement. BofQ submits that EFTPOS access issues faced by smaller card issuing institutions relate more to the imbalance of transaction costs that they bear compared to the larger card issuing institutions as they are unable to negotiate equivalent (volume based) interchange fee arrangements. BofQ further submits that, in the short term, the most effective form of competition in card issuing will come from existing participants as it does not consider that a new entrant could effectively provide the same level of competition to the larger card issuers as that of the existing participants.

Merchant acquiring

- 5.17 The Applicants consider the proposition that fixing the interchange fees at zero removes an incentive for existing issuers and acquirers to deal with a new entrant to be flawed. In particular the Applicants consider that other factors are important in such a decision, and those other factors can be used by a new entrant to win access without the need to rely upon accepting a disadvantageous interchange fee. Further the Applicants consider that fixing the interchange fees at zero will remove a potential hurdle to a new entrant as an incumbent will not be able to discriminate against a new entrant by imposing an interchange fee which is disadvantageous relative to the new entrant's competitors.
- 5.18 The Applicants also consider that the draft determination fails to explain why a card issuer, who had an incentive to negotiate an agreement with a new entrant acquirer under the present arrangements, would cease to have an incentive to negotiate an equivalent agreement under a zero interchange fee regime. The Applicants submit that, under the proposed conduct, the only relevant difference would be that card issuers are relieved of a payment stream to acquirers in general. The Applicants consider that under the proposed arrangement a card issuer would require a new entrant acquirer to provide less incentive in order to achieve a successful bilateral agreement. The Applicants also consider that the draft determination does not explain why an incumbent issuer would be deterred from accepting a payment.
- 5.19 The Applicants consider that the proposed arrangements will provide greater certainty as to the cost of interconnection as there will be no requirement to negotiate over the interchange fee. The Applicants submit that this is one of the means by which the proposed conduct will reduce barriers to entry.
- 5.20 The Applicants further note that, as the proposed agreement affects interchange fees received by merchant acquirers from card issuers and not fees paid by merchants to merchant acquirers, there is no reason why different pricing should not continue to be offered to merchants, depending on the balance of interests, including the potential income to be generated by a merchant.
- 5.21 The Applicants consider that the interchange fee proposal will act as a catalyst for the renegotiation of merchant service fee agreements and this will provide a strong incentive to merchants to compare alternative offers and merchants will be in a position to play acquirers off against each other. The Applicants note that, while the ability of merchants to negotiate will be influenced by their size and attractiveness to acquirers, there is no clear reason to expect that merchants in general, or small merchants in particular, will be adversely affected by the renegotiation process.
- 5.22 The Applicants also submit that the cost increase to merchants, which would be more than offset by a cost decrease associated with credit card arrangements, is a necessary part of the shift in incentive towards use of the lower cost EFTPOS system.

Public benefits

- 5.23 The Applicants consider that the Commission in its draft determination has incorrectly discounted the claimed public benefits as it has considered that competitive pressures are insufficient to ensure that issuers' cost savings will be passed on to cardholders. The Applicants submit that the Commission does not present any direct evidence to support this conclusion.

Pass through of card issuer savings

- 5.24 The Applicants submit that it is implausible that cost reductions will not be passed on to card holders in some manner. The Applicants consider that even if it were to be assumed that the relevant markets were characterised by the presence of pure monopolists, a pure monopolist card issuer is likely to reduce prices in the face of a reduction in costs, as to not do so would be to forgo increased profits through higher sales. The Applicants note that, while it may be true that a monopolist would not pass on the full reduction in costs, such a pass through would not be required in order for the proposed public benefit of reduced overall costs in the payment system to be achieved.
- 5.25 The Applicants submit that the proposed agreement will not reduce competition between card issuers, but rather, even in a market in which competition among card issuers is constrained and new entrants face high barriers to entry, a reduction in the interchange fees to zero would result in some cost savings being passed through to consumers, thereby leading to the creation of a public benefit. The Applicants consider that it ought not to be concluded that, on the basis of unspecified high levels of concentration, the savings passed on to consumers will be less than substantial.
- 5.26 The Applicants also note that, ultimately, all costs of EFTPOS are borne by consumers (not necessarily just cardholders). The Applicants submit that they have sought to limit EFTPOS cost increases by exposing these fees to greater competition than at present. The Applicants consider that by reducing interchange fees to zero, the remaining fees (being fees to cardholders and fees to merchants) are exposed respectively to competition between card issuers and competition between merchant acquirers. The Applicants consider that this competition will ensure that there is a pass through of at least some of the savings by card issuers, as either lower fees or as some other aspect of an improved price/service/quality bundle provided to cardholders.
- 5.27 In a separate submission provided at the predetermination conference, the Credit Union Services Corporation (Australia) Limited (CUSCAL) noted that its members had indicated that they intended to pass the benefit of the interchange fee cost savings on to cardholders.

- 5.28 The Australian Settlements Limited (ASL), which represents building societies, noted that its members are primarily card issuers and that its members pay substantial interchange fees to merchant acquirers. ASL considers that the proposed EFTPOS interchange fee agreement is likely to redress the imbalance between card issuers and merchant acquirers and is more reasonable than current arrangements. According to ASL, the EFTPOS interchange fees paid by its members are partially passed on to cardholders as transaction account fees (such as EFTPOS usage fees) and are partially absorbed. ASL considers that the concurrent reform of EFTPOS and credit cards is necessary, in particular as the net effect of credit card reform will be a reduction in credit card programs. ASL submits that, by aligning the credit card and EFTPOS reform processes, its members would be able to offset cardholder cost changes between debit and credit cards. ASL noted that the pass through of the EFTPOS interchange fee savings would be complex given that there are currently fee free transactions. ASL expects however that the EFTPOS reform will lead to a reassessment of current fee structures to cardholders and that the proportion of costs currently passed on as a fee to cardholders would be passed on as a saving if interchange fees are reduced to zero.

Price signals

- 5.29 The Applicants have expressed concern that interested parties have misunderstood the point at which transparency occurs, namely at the level of fees to cardholders and fees to merchants not at the level of retail prices to consumers. The Applicants note that interchange fees operate between card issuers and merchant acquirers and that it is at this point that fees are alleged to lack transparency. The Applicants submit that a move away from the relative invisibility of inter-bank payments into the more public spheres of merchant/acquirer, issuer/cardholder that the proposed arrangements seek to effect. The Applicants submit that in these spheres the fees will be transparent to merchants and to cardholders and will be exposed to competitive forces.
- 5.30 In relation to cardholder price signals (provided by card issuers) the Applicants consider that the situation in retail banking is typical of any market with differentiated products (or services) where firms compete on the basis of price / service / quality packages. The Applicants submit that it is a mistake to emphasise only price competition in a market where consumers value various aspects of a service package in different ways. The Applicants consider that it is only because there is not a narrow range of easily comparable packages on offer – which is itself a result of effective competition – that any issue of complexity for consumers exercising their choice arises.

- 5.31 In relation to merchant generated price signals, the Applicants submit that if merchants were to impose a surcharge, then the higher retail price (including the surcharge) would offset the reduction in cost of card use and thus not provide consumers with any incentive to move towards a lower cost means of payment. In this respect the Applicants note that 'lower cost of card use' refers to greater value to card users, whether that increased value is achieved through lower transactions costs or higher levels of service, while 'lower cost' refers to lower resource cost, i.e. lower cost to the overall community. The Applicants note that in this context 'lower cost' it is not a reference to the price directly faced by the consumer, although the lower resource cost should be reflected in lower consumer prices generally (not just for users of EFTPOS).
- 5.32 The Applicants further consider that by implication the Commission's draft determination has sought retail price signals that reflect (and therefore vary with) the precise cost of precise inputs. The Applicants contend that the allocation of costs and the adoption of variable prices is overly simplistic and fails to account for how businesses in competitive markets operate. The Applicants submit that all prices are set in markets and therefore reflect both supply and demand conditions (cost is purely a supply-side determinant). The Applicants contend that a change in interchange fees can no more influence a retail market on a unilateral basis than can a change in other supply costs incurred by a retailer, such as land rates.

Flexibility of interchange fees

- 5.33 The Applicants submit that interchange fees are currently neither flexible nor dynamic and have hardly changed since their introduction in the early 1990's with newer interchange fees based on earlier agreements. The Applicants consider that the proposed change in interchange fees will act as a catalyst for the renegotiation of financial institutions' agreements with merchants and consumers. The Applicants consider that this will lead to a 'shake-up' in the markets for retail and commercial banking, unsticking arrangements that have, in many cases, been in place for years and providing an opportunity for more competitive outcomes.
- 5.34 The Applicants consider that the observed inertia of EFTPOS interchange fees is a result not only of the market structure, but also of the institutional setting and past experience. In particular the Applicants submit that bilateral agreements are too difficult to change when compared with the benefit of doing so. The Applicants contend that while it may be true that the market structure also influenced the inertia, a different interchange fee-setting arrangement may have made a significant difference.
- 5.35 The Applicants note that, in the short term, the proposed conduct will result in a standardised fee but consider that the issue to be considered is whether changes in market circumstances are more likely to be reflected in changes in the interchange fee under the proposal than they were in the past. In this respect the Applicants consider that market circumstances have changed markedly, for example the Applicants submit that there is no longer a case for subsidising merchants to take up EFTPOS, but that the interchange fee has not responded.

5.36 The Applicants submit that, in rejecting the argument that the proposed conduct will introduce greater flexibility over time into the setting of interchange fees, the Commission in its draft determination has ignored the qualification of ‘over time’. In particular the Applicants note that under the proposed conduct, EFTPOS interchange fees could be multilaterally reset if there were a case for it. The process for doing so would exist where it did not before, and the costs of change would be less than they were before. The Applicants submit that the central rationale for the proposal is to set the interchange fee to zero and that it is not intended that the interchange fee level will be subsequently changed at will, but rather that such change would only occur after review by the Commission.

5.37 The Applicants consider that the setting of interchange fees at zero will in no way constrain the ability of merchants and acquirers to negotiate and renegotiate their own arrangements from time to time and notes that the ARA in claiming that the proposed arrangements for amending the level of the interchange fee (75 per cent agreement) are “*unwieldy, time consuming and less flexible*” fails to recognise that interchange fees operate between issuers and acquirers, not between issuers and merchants (unless a merchant is acting as an acquirer).

Scope of the applications for authorisation and role of the Commission

5.38 The Applicants note that the applications for authorisation are confined to the reform of EFTPOS interchange fees and do not include access reform. The Applicants note that they support access reform, but that they consider access reform to be a matter which the APCA is better placed to address. The Applicants note that the APCA is currently considering access reform and is giving the matter priority.

5.39 The Applicants submit that access reform is not relevant to the current applications and that the Commission has erred in its draft determination by discounting benefits and exaggerating detriments on the basis that access is not being reformed simultaneously. The Applicants consider that the only aspect of access that is potentially relevant to the applications for authorisation is the extent to which (if any) a reduction in interchange fees makes access any more or less difficult than it currently is. The Applicants claim that the proposal does not exacerbate any access concerns.

- 5.40 While the Applicants note that greater ease of entry would tend to result in the pass-through of a higher proportion of cost reductions, they submit that it is not the role of the Commission to insist on optimum arrangements. The Applicants consider that the Commission is seeking to maximise public benefits and that it should not seek to leverage its authorisation powers into a role of regulating the financial services sector, where legislation gives the Commission no such functions. The Applicants submit that the Commission's role is to assess whether the reduced costs of issuers (due to the reduction in the interchange fee to zero) are likely to be passed on to card holders to a sufficient degree such that – when taken along with the other impacts of the proposed conduct – they are likely to make greater use of EFTPOS relative to other forms of payment than at present.
- 5.41 The Applicants consider that the removal of an ability to offer a higher interchange fee (if entering as a card issuer) or to accept a lower interchange fee (if entering as a merchant acquirer) will not be significant having regard to the other arrangements that are required to be negotiated as part of a bilateral agreement. In particular the Applicants consider that any reduction in flexibility due to the removal of interchange fees as an element for negotiation will be more than offset by the benefit to the new entrant card issuer of knowing that it cannot be required to pay more for interchange than its competitors in order to enter the market.
- 5.42 Individual submissions were also received from the Australia and New Zealand Banking Group (ANZ) and the Commonwealth Bank of Australia (CBA) addressing the issue of access reform. The ANZ, in acknowledging that access reform was an important public policy issue, submitted that the appropriate mechanism through which it should be addressed was the APCA CECS arrangements.
- 5.43 The CBA noted that it supported access reform and that it considers that it is important to explore the different ways in which access reform could be achieved. The CBA has expressed concern that basic principles of access reform provided by the RBA fail to take into account considerations critical to the successful implementation of access reform, including:
- the proprietary nature of the EFTPOS networks; and
 - precedents for the implementation of access in other industries.

The CBA has summarised its position in relation to access reform as follows:

- any mandated initiatives in relation to access should be only those necessary to satisfy regulatory requirements in response to instances of demonstrated market failure;
- the current EFTPOS structure is one of a series of proprietary networks linked by bilaterally negotiated commercial and physical links – there is no singular EFTPOS network. The issue of EFTPOS access is one of access to proprietary networks, with their attendant ownership rights and responsibilities. This has significant ramifications for most aspects of the current debate;

- a range of precedents should be considered in framing consideration of access – the regime imposed in respect of credit card access should not be the only source of guidance to apply to EFTPOS access; and
- the legitimate business interests of CBA as the owner of its EFTPOS network and the CBA's interest in its investment in that network should be recognised in an EFTPOS access regime. An imposed access regime should not allow other parties to free ride on this investment.

Submissions by interested parties

- 5.44 A summary of the main issues raised by interested parties following the release of the draft determination, including at the pre-determination conference, is provided below.

Consumer organisations

- 5.45 Submissions commenting upon the draft determination were provided by representatives of the Australian Consumers Association (ACA) and the Financial Services Consumer Policy Centre (FSCPC). The ACA submitted that it expected that the proposal to reduce EFTPOS interchange fees to zero would result in reductions in fees for debit cardholders and that it considered that a public benefit would arise from the move away from the status quo. The ACA noted that it considered that it was highly desirable for reforms to both credit cards and debit cards to be aligned.
- 5.46 The ACA submitted that it was not convinced that denial of the EFTPOS interchange fee proposal was the best approach to ensure EFTPOS access reform. The ACA noted there were conflicting messages from regulators regarding EFTPOS reform. In particular, the RBA was concerned with interchange fee reform and the Commission was pushing for access reform as a priority. The ACA submitted that reform relating to access to the EFTPOS network should not prevent interchange fee reform from being implemented.
- 5.47 The ACA submitted that the proposed conduct would be likely to result in a net public benefit provided pass through to consumers occurred. The ACA noted that while there was strong agreement amongst the Applicants that pass through would be likely, the Commission could grant conditional authorisation and thereby place the onus on the Applicants to demonstrate that savings have been passed on to consumers. The ACA noted that it may be appropriate to have a review in three years to assess the impact of the EFTPOS interchange fee proposal.
- 5.48 The ACA also noted that merchants are the beneficiaries of credit card reform and as such it is important that credit card and EFTPOS interchange fee reform occur concurrently. The ACA expressed concern that without EFTPOS interchange fee reform consumers would not receive any benefits.
- 5.49 The FSCPC submitted that it disagreed with the draft determination and that it would be more appropriate to deal with access to the EFTPOS network through

the APCA CECS re-authorisation applications. The FSCPC submitted that delaying EFTPOS interchange fee reform and not aligning it with credit card reform would result in financial disadvantage for consumers, building societies, credit unions and card issuers. The FSCPC considered the proposal to reduce EFTPOS interchange fees to zero should be authorised by the Commission and further that consumer groups could apply pressure to ensure that access reform was achieved in the longer term.

Merchants

- 5.50 Submissions were provided by the following merchants and organisations representing merchants – the ARA, Brennan’s, Mitre 10 Home & Trade, Noni B, Ed Harry Menswear, Suzanne Grae, Collins Booksellers, Bracey’s (Lithgow), Fashion Fair, Kibblers, Best & Less, Associated Retailers, Spendless Shoes, Spark’s Shoes, Coles Myer, Caltex, McDonalds Australia and Woolworths.
- 5.51 The ARA notes that, while it supports the draft decision to deny authorisation to the interchange fee proposal, it considers that no link exists between EFTPOS interchange fee reform and access reform to the EFTPOS network. The ARA submits that the Commission must reach its decision based solely on the merits of the applications before it and considers that the process of access reform must be kept separate and distinct from any determination in relation to the current applications dealing with interchange fee reform. The ARA considers that the proposal to reduce interchange fees to zero results in no public benefit regardless of whether access to the EFTPOS network is addressed. In particular the ARA submits that as the proposal seeks to just “shift who pays and how that happens” it will not of itself result in any increases in efficiency.
- 5.52 The ARA acknowledges that access reform is required in the EFTPOS network and that such reform is the best way to achieve long-term cost reductions and efficiency gains for all stakeholders. In particular the ARA considers that increased competition from new entrants will promote the use of modern, lower cost technology platforms, provide incentives for processing and administration cost reductions, which will in turn lead to sustainable lower costs for EFTPOS merchants and cardholder.
- 5.53 The ARA notes that the access reform process is likely to take a considerable period of time, and that the outcome of this process is not known at this time. The ARA further considers that the APCA is not the appropriate body to conduct the process of access reform and notes that it may have some conflict of interest in managing the access reform process as many of its members may suffer some commercial disadvantage if new competitors are more freely able to enter the EFTPOS market. The ARA further considers that the APCA has inappropriately ruled out considering network architecture which is a fundamental factor limiting access and new rules should be built around this.
- 5.54 The ARA submits that, in its view, the potential savings to consumers have been overstated as the bulk of the \$150 million paid per annum in EFTPOS interchange fees is transferred between the four major banks, and therefore