

Submission

to the

Ministry of Business,
Innovation and Employment

on the

Issues Paper: Retail
Payment Systems in New
Zealand

2 February 2017

About NZBA

1. NZBA works on behalf of the New Zealand banking industry in conjunction with its member banks. NZBA develops and promotes policy outcomes that contribute to a strong and stable banking system that benefits New Zealanders and the New Zealand economy.
2. The following sixteen registered banks in New Zealand are members of NZBA:
 - ANZ Bank New Zealand Limited
 - ASB Bank Limited
 - Bank of China (NZ) Limited
 - Bank of New Zealand
 - Bank of Tokyo-Mitsubishi, UFJ
 - Citibank, N.A.
 - The Co-operative Bank Limited
 - Heartland Bank Limited
 - The Hongkong and Shanghai Banking Corporation Limited
 - Industrial and Commercial Bank of China (New Zealand) Limited
 - JPMorgan Chase Bank, N.A.
 - Kiwibank Limited
 - Rabobank New Zealand Limited
 - SBS Bank
 - TSB Bank Limited
 - Westpac New Zealand Limited.

Background

3. NZBA welcomes the opportunity to provide feedback to the Ministry of Business, Innovation and Employment (**MBIE**) on the Issues Paper: Retail Payment Systems in New Zealand (**Issues Paper**).
4. NZBA acknowledges the significance of retail payments systems to the New Zealand economy and appreciates MBIE's focus and interest on these matters. NZBA looks forward to continuing the open and collaborative engagement it has with MBIE.
5. If you would like to discuss any aspect of the submission further, please contact:

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Executive summary

6. New Zealand's payments system is world leading in many aspects, including in its efficiency, security, robustness and the high proportion of electronic versus cash transactions. NZBA does not agree there are material inefficiencies or cross subsidies in the system or that these are at a level that warrants government

intervention. NZBA considers that regulation would not derive material benefits for participants in payment systems and would give rise to unintended consequences.

7. In support of our submissions, NZBA wishes to draw MBIE's attention to the **attached** independent economic analysis/review of the Issues Paper, prepared by Axiom Economics (**Axiom Report**).
8. NZBA believes any perceived current system imbalances are not material and could be appropriately addressed voluntarily by industry participants rather than reliance on the introduction of regulation (which, in other jurisdictions, has been known to fail to meet its objectives and has resulted in unintended consequences). NZBA suggests the following range of proactive and voluntary measures that relevant participants in the payments system could agree to implement within a reasonable timeframe:
 - a. Transparency and disclosure of key information to merchants (in particular the separation of debit and credit fees and notification of fees and changes);
 - b. Maintain, and raise awareness of merchant access to an approved dispute resolution scheme (where within existing dispute resolution scheme jurisdictions);
 - c. Ensuring premium cards continue to only be provided to consumers who expressly apply for or consent to them; and
 - d. Possible commitments from card schemes to continue to allow the current practice of switching dipped and swiped scheme debit card transactions to issuers, and the introduction of new lower interchange and processing fees for low value scheme debit transactions.
9. NZBA submits that the Issues Paper does not give sufficient weight or analysis to non-card/software related payment models, including the cost of cash transactions to all participants, when it comes to drawing its conclusions about the efficiency of card transactions.
10. NZBA considers that the Issues Paper should have taken appropriate account of the offsetting impact of surcharging when assessing the overall cost to merchants of accepting card payments (and changes in that cost), and that this is necessary before concluding that there are inefficiencies in the system.

Regulation not warranted

11. New Zealand's payments system is world leading in many aspects, including in its efficiency, security, robustness and the high proportion of electronic versus cash transactions. NZBA does not agree there are material inefficiencies or cross subsidies in the system, or that these are at a level that warrants government intervention. NZBA considers that regulation would not derive material benefits for participants in payment systems and would give rise to unintended consequences.
12. NZBA agrees with MBIE it is extremely important that the government fully understands the complexity and operation of New Zealand's retail payment systems before considering whether any action is required and options for action are put forward.

13. In NZBA’s view, based on its observations of the experience in other markets, a premature regulatory response could have unintended consequences, including risks that regulating interchange will not lead to price reductions being passed on to consumers, additional costs, and the potential to inhibit innovation.
14. NZBA does not believe MBIE has adequately demonstrated a market failure, or that regulation is warranted. Without further robust analytical confirmation, NZBA does not accept the assertions made in the Issues Paper regarding the nature, burden or quantum of the inefficiencies identified in the New Zealand payments system.

Independent economic analysis

15. In support of our submissions, NZBA wishes to draw MBIE’s attention to the **attached** Axiom Report.
16. Specifically, NZBA endorses the Axiom Report’s view that the Issues Paper does not provide a robust rationale for market intervention:¹

We do not consider that the analysis in the Issues Paper provides a sufficient basis to conclude that either credit or debit card interchange fees are currently too high (or could become so), or that overall economic welfare would be enhanced by controlling the level of those fees through regulation. In our opinion, much more work would need to be done before a robust rationale for regulatory intervention could be established.

17. NZBA also endorses the significant concerns raised in the Axiom Report regarding:
 - a. the analytical flaws in the Issues Paper, including:
 - i. the asserted \$45m per annum of additional costs to the economy from the use of more expensive card networks (and the methodology used to arrive at this sum);
 - ii. the asserted increased prices for all consumers to the tune of \$187m per annum to fund credit card rewards (and the methodology used to arrive at this sum);
 - b. the potential effects of interchange fee regulation, including the experience of interchange regulation in the Australian market and its outcomes – specifically Axiom’s conclusion that the Reserve Bank of Australia’s (**RBA**) intervention made credit cardholders “*unambiguously worse off*”² and the conclusion that there is no compelling evidence to suggest that the RBA’s interventions have improved overall welfare for Australians.

¹ Axiom Report, page xvi.

² Axiom Report, page vii.

Proposed proactive and voluntary measures

18. NZBA believes any perceived current system imbalances are not so material as to warrant regulatory intervention, because of the high risks of unintended consequences and rigidity associated with such intervention. Therefore, rather than the introduction of regulation, NZBA proposes the following range of proactive and voluntary measures that relevant participants in the payments system could agree to implement.
19. NZBA is firmly of the view that these voluntary measures should be fully implemented and reviewed before regulation of any kind is considered.
20. Participants would need to agree reasonable timeframes to implement these changes and, while adoption would be voluntary, we believe that competitive pressures and the desire to facilitate innovation would quickly ensure widespread adoption across the industry.

Transparency and disclosure of key information

21. A commitment from acquirers to offer transparent merchant pricing options across the market, including:
 - a. Acquiring institutions will provide key acquiring related information to merchants, including information on cancellation and renewal of terms and conditions.
 - b. This information will be disclosed in a way that is clear and simple.
 - c. Acquirers will make information about interchange rates set by schemes available to customers. In particular merchant statements will separately identify fees for debit and credit.
 - d. Acquirers will disclose their fees, fee structures and the costs to individual merchants in a clear and accessible form, and, subject to notification by the schemes, provide a reasonable minimum period of notice (to be determined) of changes to fees and/or fee structures.
22. NZBA believes that greater pricing transparency would benefit merchants, particularly in the debit market. Some of NZBA's members already provide a range of pricing options for merchants. These vary between members but include blended, unblended and unbundled pricing options and the unbundling of contactless debit from credit pricing.
23. NZBA supports an appropriate transition timeframe to allow acquirers the necessary time to make relevant technology and system changes to deliver these greater transparency measures. We suggest 12-18 months based on our members' experience of developing and implementing enhancements of these types.

Dispute resolution

24. Each acquirer will ensure that merchants continue to have access to, and raise awareness of, an approved dispute resolution scheme (as defined in the Financial

Service Providers (Registration and Dispute Resolution) Act 2008) for the investigation and resolution of complaints.

Premium cards

25. Issuers will continue to provide premium cards only to consumers who expressly apply for or consent to such cards.

Possible commitments from card schemes

26. Currently, magnetic swipe or chip (dipped) debit transactions performed on scheme debit cards are routed to the issuer (not an acquirer) via the domestic debit network and therefore, like proprietary EFTPOS, do not attract scheme fees and interchange. NZBA proposes that commitments be sought from the card schemes that they will continue to allow the current practice of switching dipped and swiped scheme debit card transactions to issuers, in order to provide certainty to the market.
27. The potential introduction of new lower interchange and processing fees for low value scheme debit transactions combined with improved pricing transparency, would likely generate growth and innovation via lower pricing. This could be achieved by discussions with industry stakeholders to investigate ways to introduce new lower interchange categories for low value transactions.

Non-card/software related payment models

28. NZBA submits that the Issues Paper does not give sufficient weight or analysis to non-card/software related payment models, including the significant cost of cash transactions
29. NZBA expects software related payment innovation should, over time, provide strong competition for card-based payments, and help to address several of the concerns outlined in the Issues Paper.

Surcharging

30. NZBA considers that the Issues Paper should have taken appropriate account of the offsetting impact of surcharging when assessing the overall cost to merchants of accepting card payments (and changes in that cost), and that this is necessary before concluding that there are inefficiencies in the system.
31. In NZBA's view, the Issues Paper does not take full and appropriate account of the offsetting impact of surcharging by merchants since it was first permitted in 2009. All merchants have the option of fully recovering their card acceptance costs and many choose to do that. Surcharging is now common across a number of categories such as airlines, accommodation, utilities, government agencies and the taxi sector. Merchants that have chosen not to implement surcharges in many cases have made a decision that accepting the sale and associated merchant service fee is preferable to the risk of not making that sale at all.
32. We also note that there are many examples where the level of surcharging appears to exceed the merchant's actual Merchant Service Fee. This has resulted in

additional costs being borne by consumers, above the cost of supply of card services to the merchants.

33. When surcharging was permitted in Australia, alongside interchange regulation, surcharges often significantly exceeded the actual merchant fee charged by the acquiring bank. This generated negative consumer sentiment, some of which was directed at banks which do not set surcharges, and led to further regulation in order to limit the level of surcharging to the actual cost of supply.
34. It would be inaccurate to draw conclusions on merchants' overall cost of accepting payments, and any movements in those costs, without accounting or allowing provision for the offsetting impact of surcharging. NZBA's view is that a considered examination of surcharging in the New Zealand market would highlight that the overall level of surcharges exceeds the movements in average interchange since the settlements with the Commerce Commission in 2009.