



American Express Australia Limited
12 Shelley Street
Sydney NSW 2000
Australia

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Via email: fsi@fsi.gov.au

Mr David Murray AO
Chair
Financial System Inquiry
GPO Box 89
Sydney NSW 2001

Dear Mr Murray,

Financial System Inquiry 2014 Submission

American Express welcomes the opportunity to comment on payment system regulation as part of the Financial System Inquiry.

1. About American Express

American Express Company is one of the largest global payment providers. The company issues credit, charge and prepaid cards and acquires its own transactions, as well as working with bank partners to issue cards in 136 countries. The company has experience with a broad spectrum of payment and financial services legalisation globally. The feedback in this submission is given in that context.

American Express began trading in Australia as a travel services company in 1954 and started issuing Australian currency payment cards 20 years later. In the past decade American Express heavily invested in its Australian operations resulting in the launch of numerous new products issued by American Express and our bank partners.

We understand that the Financial System Inquiry will look at the full scope of payments as part of its review. American Express' submission focuses specifically on credit card payments. However, we believe that our submission is equally applicable to other payment systems.

2. Payment System Regulation in Australia

2.1 Wallis Report

There has been significant investigation and regulatory initiatives in the payment space in Australia particularly since 1997 when the Wallis Report recommended that¹:

- (a) the Reserve Bank of Australia (**RBA**) should retain responsibility for the regulation of the payments system;
- (b) a new subsidiary board, the Payments System Board (**PSB**), should be established within the RBA to promote the efficiency of the payments system.
- (c) interchange arrangements should be reviewed by the PSB and the Australian Competition and Consumer Commission (**ACCC**); and
- (d) the ACCC should also monitor the rules of Visa and MasterCard.

2.2 *The Payment Systems (Regulation) Act*

The passing of the Payment Systems (Regulation) Act (**PSR Act**) in 1998 granted the RBA through the PSB wide ranging powers to designate payment systems then to:

- (a) impose an access regime on the participants in the designated payment system; and
- (b) make standards to be complied with by participants in the designated payment system,

if the PSB considers this to be in the public interest.

The PSB's powers under the PSR Act give it broad powers to regulate all payment systems.

2.3 *The credit card regulatory framework*

Following the Wallis Report and PSR Act, the PSB and ACCC conducted the review into the credit card interchange and other rules of Visa and MasterCard². Following this review the PSB commenced the process in 2001 which led to the 3 main regulatory reforms of the Australian credit card payment system:

- (a) from August 2002, the merchant pricing standard which removed the no-surcharge rules of Visa and MasterCard;

¹ <http://fsi.treasury.gov.au/content/downloads/FinalReport/chapt09.pdf>

² <http://www.rba.gov.au/payments-system/resources/publications/payments-au/interchg-fees-study.pdf>

- (b) from November 2003, the interchange standard which currently caps the weighted average interchange on credit card transactions at 0.50% and provides an authorisation to Visa and MasterCard under the Competition and Consumer Act 2010 from what would otherwise may be anti-competitive behaviour; and
- (c) from February 2004, the access standard which sets out requirements for access to issue and acquire on the Visa and MasterCard networks.

At the same time American Express entered into a voluntary undertaking to also remove their no-surcharge rules. However, given that American Express did not have collectively set interchange fees, the PSB decided that regulation of payments between American Express and its bank partners would not improve the overall efficiency of the payments system³.

2.4 *Variations to the credit card regulatory framework*

Since the initial credit card reforms in 2003 and 2004 each of the standards has been reviewed and amended, or is the process of being amended.

For example:

- (a) the merchant pricing standard was amended in 2013 to restrict the ability of merchants to surcharge only to the reasonable cost of acceptance;
- (b) the interchange standards were amended in 2006 and 2009 to provide a common interchange benchmark between Visa and MasterCard and to provide the RBA with powers to exempt Visa and MasterCard from certain requirements.

The PSB has significant powers under the PSR Act to amend or create new standards where it considers it is in the public interest.

2.5 *Other payment systems*

The PSB has used its powers under the PSR Act to make similar reforms it believes are in the public interest with other payment systems.

For example, it has designated and made standards for other payment systems such as EFTPOS, Visa Debit and the ATM network.

These examples show that the PSB through the PSR Act have the necessary powers to regulate the broader Australian payments system.

³ <http://www.rba.gov.au/media-releases/2005/mr-05-02.html>

3. American Express' position on further payment system reform

Although most of the credit card payment systems reforms for credit cards were directed at Visa and MasterCard, these reforms have either directly or indirectly had a significant impact on American Express as the niche premium network in the Australian credit card payment system.

American Express believes that the credit card reforms resulted in significant re-distribution of value from consumers and financial institutions to large merchants. Consumer credit became more costly in the form of increased fees and increased surcharging at the point of sale, particularly in monopoly markets where natural competitive pressure was limited.

However, it is not the intent of American Express to use this inquiry to seek any redress or create further time and resource intensive reviews into the PSB reforms into the Australian credit card payment system or other payment systems.

It is clear is that the rate of change within the payments system is rapidly increasing. Technology is enabling safer, faster, and more inclusive payment methods, and in many instances Australia is ahead of the rest of the world in adopting new technologies, such as with contactless payments.

As noted above, the PSB already has significant powers under the PSR Act to take any action it considers to be in the public interest whether with credit cards or with other existing or new payment systems.

American Express seeks that after such a period of significant reform, the industry is allowed to work within the current regime and focus on product innovation – especially in the mobile wallet space – rather than spend the next decade working within a further shifting regulatory landscape.

The 2013 amendments to the merchant pricing standard and the current review into the access standard show that the PSB has the powers it needs to amend the standards applying to a payment system when it considers necessary.

Further, the outcome of the PSB's Strategic Review of Innovation has already resulted in same day settlement of direct entry payments between the payment system participants⁴. The payments industry is currently working towards further innovations such as:

- (a) the ability to make real-time retail payments;

⁴ <http://www.rba.gov.au/media-releases/2013/mr-13-24.html>

- (b) the ability to make and receive low-value payments outside normal banking hours;
- (c) the ability to send more complete remittance information with payments; and
- (d) the ability to address payments in simple manner.

These outcomes demonstrate that the current regulatory framework can respond to issues which the PSB considers to be in the public interest without further need for significant reforms.

4. Finally, a word on the advantage myth

There is a misconception, largely perpetuated by the dominant card schemes Visa and MasterCard, that American Express has obtained an unfair advantage from the PSB's credit card reforms. This is simply not substantiated by fact. This argument negates the significant investments made by American Express in the Australian market, and fails to understand the nature of the voluntary undertakings made by American Express.

As stated above, American Express never levied collectively set interchange fees and the RBA has previously acknowledged that regulation of payments between American Express and its bank partners would not improve the overall efficiency of the payments system⁵.

As the two dominant card schemes in Australia still control approximately 80 percent of the market, it is hard to credit the assertion that there is an unlevel playing field that impairs their business model and that more regulatory intervention into credit card payments is required to redress the balance in their favour.

We are happy to discuss these items in more detail. Please contact John Galletta in our General Counsel's Office on +61 2 9271 1817 or john.galletta@aexp.com for further information.

Yours respectfully,



Rachel Stocks
Managing Director, Australia and New Zealand

⁵ <http://www.rba.gov.au/media-releases/2005/mr-05-02.html>