

AN ACCESS REGIME FOR THE ATM SYSTEM

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Reserve Bank

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An Access Regime for the ATM System

1. Introduction

For some years the Reserve Bank and industry participants have been working together on a reform package for the ATM system, with this package due to come into effect on 3 March 2009. The Bank's role in the reform process has been primarily to focus discussion on the need for improvement in current arrangements and to facilitate cooperation and compromise between the disparate parties that make up the ATM industry. Notwithstanding this role, the industry recently requested that the Bank use its regulatory powers to give legal certainty to the reform package. While the Bank would have preferred a solution that did not involve regulation, it is prepared to introduce an access regime to give effect to key parts of the reform package.

This document discusses the reform package and sets out the Bank's analysis and reasoning leading to its decision to implement an Access Regime.¹ In the Bank's view, the reform package, including the complementary changes to access arrangements being made by industry participants, will deliver significant benefits for consumers. In particular, the reforms will improve competition among the suppliers of ATM services, increase the availability of ATMs, and increase the transparency of the fees that cardholders are charged for withdrawing cash from an ATM. Without the reforms, there is a significant risk that the number of ATMs in Australia will decline over time, as non-bank owners of ATMs find it unprofitable to deploy and service machines.

Notwithstanding these benefits, over the next year or so the Bank is seeking more fundamental changes to the infrastructure supporting the ATM system which should ultimately render aspects of the Access Regime redundant. In particular, in the Bank's view new entrants to the ATM system should be able to connect to the system with one link using a common message standard, rather than the current requirement for a multiplicity of links using multiple, often incompatible, message formats. The need for further improvements to the current arrangements provides important context for the way the Access Regime has been constructed, with the Bank viewing aspects of the Regime as relatively temporary in nature and necessary to ensure the benefits of the industry reform package are obtained, rather than an endorsement of current practices.

The next section provides some background on the ATM system in Australia and the need for reform, with Section 3 outlining the key elements of the reform package that has been developed by the industry. Section 4 presents the elements of the Draft Access Regime that has formed the basis for consultation, while Section 5 covers the views on that Regime expressed in consultation and the Bank's response to those views. Section 6 presents the Bank's analysis of why the imposition of the Access Regime is in the public interest. The final Access Regime is provided in the attachment.

¹ *This paper should be read in conjunction with the earlier Consultation Document on the draft Access Regime issued on 10 December 2008. See http://www.rba.gov.au/PaymentsSystem/Reforms/ATM/ConsultDocDec2008/a_consultation_doc_122008.pdf*

2. The ATM System and the Need for Reform

2.1 The ATM system in Australia

The Australian ATM system is comprised of a number of ATM ‘networks’, linked together through a series of bilateral agreements. Most of these individual networks are owned by large banks and were established to provide customers of those institutions with access to cash withdrawals and some account management functionality. There are also two ‘sub-networks’, which were set up to serve the building societies and credit unions, although these days their membership is wider. These sub-networks effectively link together ATMs of a large number of smaller institutions so that they can provide their customers with access to a larger network of ATMs. In addition, in recent years, a large number of ATMs have been deployed by owners that are not financial institutions. In total, these ‘independent deployers’ currently own around half of the 26 500 ATMs in Australia.

The interconnection of ATM networks is facilitated through bilateral agreements between network owners that allow each institution’s cardholders to use the other institution’s ATMs. Among other things, these bilateral agreements have provided for the payment of ‘interchange fees’, averaging around \$1.00 per transaction, from the card issuer to the ATM owner in compensation for the service that the ATM owner is providing to the cardholder.

As interchange fees are a cost to the card issuer, many financial institutions have charged their customers a ‘foreign fee’ when they use an ATM belonging to another financial institution. These fees are typically significantly higher than interchange fees. In recent times the four largest banks have charged \$2.00 a transaction, while some smaller financial institutions have chosen to absorb the cost of the interchange fee for their customers, effectively providing them with fee-free access to a large number of ATMs.

Further details of the ATM system are provided in *Access Regime for the ATM System: A Consultation Document* released on 10 December 2008.

2.2 The need for reform

The issues addressed in the Access Regime are part of a broader set of reforms to the ATM system being implemented by the industry, with the support of the Reserve Bank. In its entirety the reform package seeks to address two main issues that have been a cause for concern for both the Reserve Bank and industry for a number of years. These are the lack of competitive pressure on interchange fees and the access difficulties facing potential new participants.

2.2.1 *Lack of competitive pressure on interchange fees*

As noted above, an important feature of the current arrangements is the existence of bilateral interchange fees between the major participants. When the Bank studied these fees in 2000, it made two main observations.²

The first was that these fees had remained fixed for many years at the levels agreed when the links were first established and that it was very difficult for existing ATM owners and card

² *Reserve Bank of Australia and Australian Competition and Consumer Commission (2000), Debit and Credit Card Schemes in Australia: A Study of Interchange Fees and Access, October.*

issuers to negotiate different rates. The second was that, although interchange fees were paid to ATM owners as recompense for providing a service, the fees bore little relationship to the cost of providing an ATM withdrawal. The Bank found that while interchange fees averaged around \$1.00, the average cost of providing a cash withdrawal at an ATM was around \$0.50 and there appeared to be no competitive pressures to reduce interchange fees. In addition, the foreign fees being paid by cardholders for a cash withdrawal were substantially higher than the cost of providing the service and there seemed to be only limited competitive pressures to reduce that margin.

One reason why ATM interchange fees are not subject to the normal forces of competition is that bilateral interchange agreements are not easy to renegotiate. The potential loser out of any renegotiation naturally prefers the status quo, so unless the potential winner is prepared to walk away from the agreement – which may be difficult if its cardholders have become used to the convenience of access to a wider ATM network – the interchange fee is likely to remain unchanged. Experience suggests that such ‘sticky’ interchange fees are a common feature of bilateral payment systems.

A second reason is that cardholders have no influence over these fees. Although interchange fees have a bearing on foreign fees, customers face the same foreign fee from their financial institution regardless of the interchange fee paid. They therefore have no incentive to favour ATMs with lower interchange fees. This in turn means that there is no incentive for ATM owners to lower their interchange fees to promote use by cardholders. More generally, the uniformity of foreign fees reinforces the observation that the relationship between interchange fees and the costs of providing ATM withdrawals is weak.

This weak relationship between fees and costs raises a potentially important issue going forward. Because of the difficulties with renegotiating bilateral interchange fees, these fees may remain at their current levels even if costs rise. As a result, there is a risk that many ATMs will become uneconomic over time. Indeed, the Bank estimated in 2007 that the average cost to an ATM owner of providing the service of a cash withdrawal was around \$0.75, up from \$0.50 in 2000. As costs continue to rise, it is likely that the number of ATMs – particularly those operated by the independent deployers – will decline if interchange fees are not renegotiated. This would result in less convenience for consumers and reduced public benefit from the ATM system.

2.2.2 *Access difficulties*

The second issue with the current bilateral arrangements is the difficulties faced by new entrants in gaining access to the system. These difficulties are similar to those identified by the Bank with respect to the EFTPOS system and which were addressed in a co-regulatory framework by the Bank and the Australian Payments Clearing Association (APCA) in 2006.

The bilateral arrangements in the ATM system make access complicated in three main ways. First, any potential new provider of ATM services that wants to be a direct participant in the system must separately approach existing participants to negotiate agreements to establish connections. Each individual agreement tends to be different with respect to technical and business requirements, further complicating the negotiation process and increasing costs.

Second, existing direct connectors have little incentive to facilitate entry since the prospective entrant is likely to be a competitor in at least some aspects of the participant's business and, in the case of smaller new entrants, might offer existing participants only limited benefit in terms of network expansion. This means that participants may either refuse to negotiate or delay the process. Even if an in-principle agreement to connect is reached, there are no standardised procedures around testing or guidelines around timing. As a consequence, the incumbent may effectively hold up entry by delaying the technical work required. In addition, there is no standard cost of connection nor is the cost of connection known in advance, so new entrants may find it difficult to build a robust business case.

Third, in a bilateral system, the need to negotiate the interchange fee to be paid can also act as a barrier to entry. At its most prohibitive, the inability of a new entrant to negotiate an interchange fee would prevent it from participating in the system. But even if the other participants are prepared to negotiate an agreement, the new entrant may find that the only interchange fee the incumbents are prepared to consider is at a level that would render the new entrant uncompetitive. If, for example, the owner of a new ATM network found that other participants were only prepared to pay it \$0.50 for use of its ATMs by cardholders when other ATM owners were receiving \$1.00, it would immediately be at a competitive disadvantage to other participants. Bilateral interchange fees therefore effectively act as a price of access.

3. The Reform Package

Reflecting the concerns set out in the previous section, the Bank has been working with the industry for a number of years to reform the ATM system. The history of those efforts was set out in the earlier Consultation Document. These efforts ultimately led to a reform package being developed by the industry with the following elements:

- (a) an industry-developed access code implemented through APCA;
- (b) ATM owners having the freedom to charge cardholders directly for the use of an ATM, with any charge being disclosed to the cardholder prior to the withdrawal being made;
- (c) zero interchange fees between direct connectors;
- (d) sub-networks being able to retain their multilateral interchange fees;
- (e) an ability for institutions to enter into arrangements to rebate the direct charge for their customers at the time of the transaction; and
- (f) a dispute resolution and disclosure regime.

The Bank's analysis of this package is that it addresses the two central problems discussed above.

In particular, the move to a regime in which ATM owners directly charge cardholders rather than earn revenue through interchange fees will increase competition in the provision of ATM services. With the price of an ATM withdrawal clearly displayed there is an opportunity for the normal forces of competition to come to bear. Where an ATM is charging a fee above the cost of provision in many cases it will be possible for a competitor to put an ATM with a lower fee near the high-fee ATM. These competitive forces would be expected to lower the cost of ATM

services below what they would otherwise be. In addition, the access reforms will make it easier for new firms to enter the market, strengthening these competitive forces.

The reform package will also increase the transparency of the price of ATM services. Customers will be made aware of the price of a foreign ATM withdrawal at the time of a transaction and given an opportunity to cancel the transaction if they are not prepared to pay the fee. This will be a significant improvement over the current situation where the fee for using a foreign ATM is included on the account statement usually well after the time of the transaction.

The package will also promote choice and the provision of ATM services in areas that do not currently have ATMs. Direct charging allows ATM owners to place ATMs in locations that were uneconomic under the one-size-fits-all interchange fee system. This means that low-demand locations are likely to get ATMs that they would not have in the past – increasing choice and convenience for consumers. A related benefit is the potential for ATM deployers to offer different services through their ATMs that were difficult to accommodate under the fixed interchange fee system.

4. The Draft Access Regime

The new arrangements for the ATM industry are the outcome of many years of work by the industry and the Reserve Bank. With the broad details of the package being developed by industry participants in consultation with the Bank it had been hoped that the reforms could be implemented entirely by the industry, without the need for regulation. This, however, has not proved possible. While the industry, under the auspices of APCA, has been able to finalise an Access Code that addresses the rights and obligations of access seekers and access providers, and has developed and implemented the technical arrangements necessary for direct charging, it came to the view in late 2008 that the most effective way of providing legal certainty to two elements of the package was through regulation by the Bank. These elements relate to the arrangements for setting interchange fees to zero and to the establishment of a cap on the cost of connection to the ATM system. Given that both these elements affect the ease of access for potential participants to the ATM system, the Bank is implementing the necessary regulations through an access regime (rather than a standard) under Section 12 of the *Payment Systems (Regulation) Act 1998*.

A Draft Access Regime was released by the Bank for consultation on 10 December 2008. This draft Regime addressed three main features of the ATM system: the cap on connection charges; the establishment of zero interchange fees (with some exceptions); and the transparency of arrangements under which interchange fees continue to be paid.

4.1 Connection charges

The connection charge is the charge that an incumbent may apply to a new direct connector in the ATM system in order to establish and test a connection that will allow the new entrant to exchange transaction messages and clear and settle ATM transactions with the incumbent. A new entrant wishing to participate fully in the ATM system would need to establish direct connections and pay fees to all existing direct connectors. The cap to be set under the Access

Regime seeks to limit that cost to that of an efficient provider of access and also provide some certainty for potential entrants.

The proposed cap of \$76 700 included in the Draft Access Regime is the lowest cost of providing a direct connection estimated in a survey of anticipated direct connection costs undertaken by APCA in mid 2008. An alternative suggested by some participants was to use the average cost of connection from the survey, which would be around \$200 000. The Bank's choice of the lower cap reflected a balancing of the interests of both current and prospective participants as well as being the methodology adopted for setting a cap on the cost of EFTPOS connections in the EFTPOS Access Regime. While this means that some existing participants would not be able to cover fully the cost to them of establishing a new connection, it also means that new entrants wishing to establish multiple connections would not be required to meet additional costs associated with the complexity or inflexibility of some participants' systems. At the same time, an incentive would be provided to existing direct connectors to adopt more efficient systems.

The Draft Access Regime did not provide for a review of the direct connection cap. This reflected the Bank's view that the network architecture and associated access arrangements will need to change in the period ahead to allow new entrants to access the system with a single connection and minimal bilateral negotiation. A move to access arrangements of this type should largely eliminate the need for bilateral connection charges.

The Consultation Document also noted that the Bank was of the view that no fee should be charged for the establishment of a direct clearing/settlement arrangement. This is an arrangement that allows two parties that are indirectly connected via a switch to directly clear and settle ATM transactions between them. The Bank views clearing and settlement as fundamental banking business and, provided financial institutions meet appropriate objective prudential standards, they should have the right to clear and settle directly with other financial institutions, with each institution meeting its own costs (including any fees for membership of the access company and the clearing system for ATM transactions).

4.2 Interchange fees

The Draft Access Regime would eliminate interchange fees between the direct connectors that form the core of the ATM system. However, the Bank has been conscious that interchange-like fees can be pro-competitive in some circumstances where they apply outside the group of direct connectors. In particular, fees which allow small institutions access to a larger network of ATMs than they would be able to provide themselves, free of direct charges, may help those institutions to compete on a more equal footing with the larger players in the industry. To that end, the Draft Access Regime allowed interchange fees to be paid between members of a sub-network – in line with the original industry proposal. The Draft Access Regime also allowed institutions to establish one-way arrangements whereby they pay a per-transaction fee to an ATM owner so that their customers can access those ATMs without a direct charge being levied. Under a one-way arrangement, those institutions could not provide reciprocal arrangements to the ATM owner. A single one-way arrangement is sufficient for a small institution to gain access to a network of ATMs of a similar size to the major banks, free of direct charges. The Draft Access Regime therefore limited an institution to a single one-way arrangement to access another party's

ATMs. An important consideration in setting this restriction was the desire to avoid a renewed proliferation of bilateral interchange fees.

In the Bank's view, the alternative of not allowing interchange fees in any circumstances would place small financial institutions at a significant competitive disadvantage since customers would be attracted to the larger banks' ability to offer a wide network of ATMs to their customers free of direct charges. Smaller institutions could not hope to replicate those networks.

4.3 Transparency

The above arrangements for allowing interchange fees in limited circumstances were supported in the Draft Regime by transparency provisions. In order to ensure that access arrangements for sub-networks are open and transparent, the Draft Regime required any multilateral interchange fee within a sub-network to be publicly disclosed and the rules governing access to that sub-network to also be published. In addition, it required one-way arrangements to be reported to the Reserve Bank shortly after the introduction of the Regime or within 30 days of the establishment of a new arrangement. This would allow the Bank to monitor the use of such agreements and compliance with the Regime. The proposed transparency arrangements should impose minimal compliance costs on participants.

5. Consultation

As previously noted, the ATM reform process has involved extensive consultation with industry over many years. In particular, the industry proposal that is supported by the Regime is the product of an intensive round of discussions and consultation that took place through 2006 and 2007. As such, many issues have been canvassed and considered in those earlier rounds. This section focuses on the particular issues related to the draft Access Regime. Details on earlier discussions can be found on the Reserve Bank's website as set out in media releases, consultation documents, industry submissions and industry discussion papers.

5.1 Views expressed during consultation

The Consultation Document requested submissions from interested parties by 16 January 2009. The Bank received thirteen submissions – from industry bodies, a consumer advocacy group, organisations representing people who are blind or vision impaired, and a number of participants in the ATM system, including banks, independent deployers and a sub-network operator. Eleven of the parties making submissions chose to meet with Bank staff to further discuss their views.

As might be expected given that the industry has requested regulation by the Reserve Bank, submissions were generally supportive of the proposal to set an Access Regime and of the ATM reform package more generally. Other comments largely related to the setting of the cap on the direct connection charge and the Bank's view that there should be no charge for establishing a direct clearing/settlement arrangement. There were also some calls for greater flexibility in the provisions relating to interchange fees.

The banks, the Australian Bankers' Association (ABA) and APCA questioned the proposal to set the cap on the direct connection charge at the lowest cost of respondents to the APCA connection cost survey. They argued that this approach is biased toward access seekers because

all but one access provider would be required to subsidise new entrants. Some also suggested that the variation in connection costs in the survey reflects the size and complexity of institutions' operations rather than efficiency, undermining the usefulness of the lowest-cost respondent. Submissions from the largest banks suggested that the average cost of connection from the survey be used, rather than the lowest cost, with the ABA noting that this approach would still provide access providers with an incentive to reduce costs.

A non-bank payments service provider supported setting the cap at the lowest cost in the survey, while a regional bank noted that it would be difficult to adopt a significantly different approach to that adopted in the EFTPOS system.

APCA suggested that setting a direct connection cap that is too low might lead to the establishment of connections that are inefficient because they do not generate sufficient volume of transactions to justify establishment and operation. Similar arguments were made in relation to direct clearing/settlement arrangements. APCA proposed that a 'peer or pay' model be adopted, under which additional charges would apply if, after a period of time, certain volume thresholds had not been met.

A number of bank submissions, along with those from the ABA and APCA disagreed with the Reserve Bank's view that there should be no charges for establishing direct clearing/settlement arrangements. They argued that there are significant costs involved in establishing these arrangements, which access providers should be permitted to recover. APCA argued that direct clearing/settlement arrangements should not be viewed as distinct from direct connection arrangements because, in most respects, they are identical; the only point of difference is physical connectivity between access provider and access seeker.

Most banks indicated a preference for a direct clearing/settlement cap based on the average direct clearing/settlement cost in the APCA survey. APCA again suggested a 'peer or pay' model.

One submission supported the notion that the right to clear and settle is a 'basic need' of the payments system and should not incur a charge. It was also noted in discussion that this outcome could not practically be achieved unless it was explicitly addressed in the Access Regime. The same party also called on the Bank to review direct clearing/settlement arrangements for the EFTPOS system.

Most submissions supported the general approach to interchange fees taken in the draft Access Regime, although several argued for some additional flexibility to allow for circumstances where interchange fees might be beneficial. One major bank argued that prohibiting the payment of interchange fees between direct connectors is unnecessarily prescriptive and might prevent the emergence of new and innovative business models. Similarly, another suggested that the draft Access Regime be changed so that, rather than eliminating interchange fees, it instead set interchange fees to zero to provide flexibility if necessary to advance ATM reform. APCA suggested that a provision be included in the Regime that would allow the Bank to approve interchange arrangements that enhance competition.

Some submissions specifically noted their support for allowing interchange fees within sub-networks and for one-way arrangements. One submission argued that smaller institutions

should be permitted to have in place two one-way access arrangements. Few submissions commented on the transparency provisions of the draft Access Regime, but those that did supported the approach taken.

While not specifically part of the current regulatory process, a number of submissions commented on two further issues raised in the Consultation Document. The first was the Bank's suggestion that it would consider taking a more active role in ATM access arrangements if further improvements in the access model have not been achieved by March 2010. Characteristics identified by the Bank as important for indicating progress included: the establishment of a single point of access for new entrants, minimising the extent to which negotiation with multiple participants is required; the use of message formats that are standardised to the fullest extent possible; and the use of international standards where appropriate. Submissions that commented on this issue tended to be supportive of the overall objective, with some pointing to developments that were already taking the industry in the desired direction. This included the work of APCA in this area and the establishment of a 'community of interest network' (COIN) by two of the major banks. However, some banks expressed concern about the Bank's timetable, in one case suggesting that considerable work needed to be undertaken on the underpinnings for new network arrangements and in another that the timing of investment is driven by other factors. One submission argued that the prospect of obtaining access through a single connection in a year's time would deter potential entrants from seeking access in the coming year.

The second issue addressed by several submissions, but not directly related to the proposed Access Regime, was the level of foreign fees. Some submissions argued that banks will continue to face a number of costs from foreign ATM transactions when interchange fees are eliminated, including for transaction processing, dispute resolution and fraud, and that it was appropriate that banks be able to recoup these costs through foreign fees. Another submission argued that the cost to issuers of foreign transactions was likely to be only a few cents and that the imposition of a material foreign fee would undermine elements of the reform process. The Consumer Action Law Centre argued that the Access Regime should be extended to explicitly address pricing to customers – preventing the charging of foreign fees where no interchange fee is levied and placing constraints on direct charges.

Some submissions also raised what they felt might be unintended consequences of direct charging. The Consumer Action Law Centre noted that the application of direct charges to balance enquiries could discourage people from verifying that they have funds available before making a withdrawal. It suggested that ATM owners be required to provide a warning screen if a transaction would lead to an overdrawn account.

Blind Citizens Australia and Vision Australia raised concerns about the ability of blind and vision-impaired people to use audio-enabled ATMs (which provide audio instructions to assist transactions) when direct charging is introduced. They were concerned that the audio software on the available ATMs might not be updated in time for the start of direct charging, rendering them unusable for blind or visually-impaired people. They were also concerned that blind and visually-impaired people tend to be highly restricted in the ATMs they can use and are therefore less likely to be able to search for an ATM from their own institution or a foreign ATM with a lower fee.

5.2 Discussion

The consultation process has demonstrated the industry's continued support for the setting of an Access Regime for the ATM system under Section 12 of the *Payment Systems (Regulation) Act*. Given this, the following discussion focuses on three main issues: the calculation of the cap on direct connection costs; whether the cost of setting up direct clearing/settlement arrangements should be capped explicitly in the Access Regime; and the exemptions for interchange fee-like payments.

The Bank has considered the argument that the surveyed connection cost upon which the direct connection charge cap is based is unrepresentative and leads to subsidisation of new entrants by all but one access provider. It remains of the view, however, that the cost paid by new entrants ought not be determined by the complexity of others' systems and that a low cost of connection is important to achieving competitive outcomes in a system where potential entrants must separately connect with a number of incumbents. If the average cost were used, as suggested by some submissions, this might imply a total connection cost of well over \$1 million for a new entrant wishing to establish a full set of direct connections. Furthermore, consistency with the EFTPOS Access Regime argues for adoption of the lowest surveyed connection cost as the benchmark. The Bank, therefore, continues to be satisfied that a direct connection charge cap of \$76 700 represents an appropriate balancing of the interests of access seekers and access providers.

The Bank has also reconsidered whether access providers should be permitted to charge access seekers for establishing direct clearing/settlement arrangements. Although there are costs to financial institutions of implementing such arrangements, the Bank remains of the view that clearing and settling are fundamental aspects of banking business and that it is appropriate that each institution meet its own costs in this area. A significant part of the public benefit accruing from the payments system stems from the ability of consumers to make payments regardless of the institution they bank with or the institution the merchant banks with. Efficient clearing and settlement arrangements are essential if these benefits are to be realised. Allowing participants to impose fees for the establishment of direct clearing and settlement arrangements would not only increase costs for new entrants but might also force some financial institutions to clear and settle indirectly through an agent who is also a competitor. While many institutions may find such agency arrangements efficient, they may hinder the ability of others to compete. On balance, therefore, the Bank is of the view that the benefits of prohibiting charges for establishing direct clearing/settlement arrangements outweigh the costs to current participants of providing that access without charge.

As noted above, the Draft Access Regime did not make any explicit reference to charges for establishing direct clearing/settlement arrangements. During consultation it was argued that this approach could present further access problems if institutions chose to impose large charges for clearing and settlement (perhaps outside of the industry Access Code). In finalising the Access Regime, therefore, the Bank has included a clause stating that parties seeking to establish direct clearing and settlement arrangements with other participants cannot be charged a fee.

In terms of interchange fees, the Bank recognises the benefits that would come from the Access Regime having some additional flexibility. The variety and complexity of business arrangements

that apply for participants in the ATM system make it difficult to be certain that the carve-outs in the draft Access Regime will cover all circumstances where payment of an interchange fee might be beneficial. Submissions have suggested that the Access Regime provide the Bank with the ability to approve interchange fee arrangements that enhance competition.

The Bank sees merit in this suggestion and has therefore included a clause in the Access Regime allowing it to grant an exemption to the interchange fee provisions and setting out the matters the Bank will take into account when granting such an exemption. Exemptions will only apply to particular arrangements and will be evaluated on the same basis as the exemptions already explicitly included in the Access Regime – that is, having regard to: whether the exemption would be in the public interest; the interests of current participants in the system; the interests of people who, in the future, may want access to the system; and any other matter the Reserve Bank considers relevant. In addition, the Bank will publish notice of any exemptions granted on its website, including the nature of the exemption and the identity of the participants involved.

The Bank sees no particular advantage to rewording the Access Regime to set interchange fees to zero, rather than simply removing them. In the event that there was a view that the new arrangements should be changed in some way, the same processes for variation of the Access Regime, including public consultation, would likely be required regardless of whether interchange fees are set to zero or abolished.

The Bank has also re-examined whether participants should be permitted to have more than a single one-way arrangement for access to another network's ATMs. Permitting small institutions to have two or more such arrangements would potentially make it possible for them to establish larger fee-free networks than the existing networks. While clearly an advantage to these institutions, it could put the whole reform process at risk by encouraging large networks to look for ways to re-establish bilateral interchange fees, thereby reintroducing the problems of the current system. The new arrangements will provide small financial institutions with the opportunity to have a fee-free network at least as large as those of the major banks while maintaining the integrity of the reforms by removing bilateral interchange fees between the main networks. In addition, small institutions may still, if they wish, absorb the cost of ATM withdrawals for their customers to provide broader fee-free access to ATMs, just as they currently do. This is a business decision for them. The Bank, therefore, does not propose to change the Access Regime to allow participants to have more than one one-way arrangement under which they access another participant's ATMs.

Finally, the Bank has noted the concerns raised by Blind Citizens Australia and Vision Australia in relation to accessibility of ATMs. The Bank encourages ATM operators to ensure that audio-enabled ATMs are updated in a timely fashion and issuers to consider rebating direct charges to cardholders who are restricted to using foreign ATMs for reasons of accessibility.

6. Regulatory Requirements and Analysis

The *Payment Systems (Regulation) Act* permits the Bank to impose an access regime on a designated payment system where it considers it appropriate, having regard to:

- (a) whether imposing the access regime would be in the public interest;
- (b) the interests of the current participants in the system;
- (c) the interests of people who, in the future, may want access to the system; and
- (d) any other matters the Reserve Bank considers relevant.

As discussed above, the Bank has considered an access regime for the ATM system at the request of the industry. The central choice for the Bank has been whether or not to proceed with a regime of this type. If it were to not proceed, there is likely to be considerable dislocation in the ATM industry, and the reform process would be delayed further, perhaps for many more years. The Bank is satisfied that the Access Regime, together with the industry-developed Access Code, is in the public interest.

The benefits of proceeding with the Access Regime and the introduction of the new arrangements fall into three categories:

- encouraging choice and convenience for customers;
- introducing transparency in pricing of ATM transactions undertaken at foreign ATMs; and
- improving competition in the provision of ATM services.

As noted in Section 2, one of the features of the current arrangements is that revenue received by ATM owners is determined by agreements entered into when the system was first established which have very little flexibility. Under these arrangements, it is therefore likely that, as costs rise over time, the availability of ATMs will decline. This would result in less choice and convenience for consumers. By providing ATM owners with the ability to price their service, subject to competition from other ATM owners, the new arrangements will ensure that ATMs continue to be widespread, including in some areas that currently may not have an ATM. Furthermore, with an ability to determine their own prices, ATM owners will have an opportunity to investigate additional services that ATMs might offer on a competitive basis.

Under the new arrangements, as is the case currently, most customers will not be charged for use of their own financial institution's ATMs and smaller financial institutions will be able to enter into arrangements with larger networks to provide fee-free access to ATMs for their customers. Where a foreign ATM is used, the fee charged by the owner of the ATM will be clearly disclosed before the cardholder makes the withdrawal. If the cardholder decides not to proceed with the transaction they will be able to cancel the transaction without charge.

With the fee disclosed up front, there will be more competitive pressure on ATM fees than is currently the case. Under the new arrangements, the cost of an ATM withdrawal may vary across locations, although it is likely that a number of banks will have universal pricing across their own networks. In high-traffic locations, where the cost of providing each ATM withdrawal is likely to be relatively low, fees might be lower than in higher-cost locations. It is important to note, however, that attempts by ATM owners to charge fees well in excess of costs is likely

to lead to a competitive response from other ATM owners, including by installing a lower cost ATM in the same area.

In the Bank's view, the benefits of these new arrangements are likely to be maximised if foreign fees are eliminated. Given the changes that are taking place, and since most institutions now provide transaction accounts which offer unlimited electronic transactions for a monthly fee, the Bank no longer sees a case for financial institutions to charge their customers these fees. While the Bank has no regulatory power over foreign fees, its view is that the pricing transparency of the system and the competitive pressures will be diluted if cardholders have to pay fees to the ATM owner and to their own institution.

Finally, the simplified access arrangements will facilitate entry to the market, further assisting in keeping pressure on fees and improving convenience for customers.

While the Bank judges that these benefits are significant, it recognises that there have been implementation costs for the industry, including: reprogramming of ATMs (and in some cases replacement of ATMs); changes to systems that support the exchange of payment messages; and customer education. These costs have been incurred across financial institutions, independent deployers and switches. Many of the costs would have been incurred even without the reforms due to the need to upgrade the ATM fleet and technology in order to ensure that Australia has a modern and up-to-date ATM system. Importantly, these costs have been incurred as part of an industry initiative, the outcome of which will ultimately be a more convenient, transparent and competitive ATM system going forward.

If the Bank were not to proceed with an access regime, there is a significant risk that the industry would abandon most, if not all, of the reform package. The Bank's liaison with industry participants suggests that a significant number of financial institutions would not be willing to proceed with a cap on the connection charge or the elimination of interchange fees in the absence of the Bank's Access Regime. In particular, some institutions are concerned that the alternative of authorisation by the Australian Competition and Consumer Commission (ACCC) would not provide the degree of legal certainty required, since the setting of zero interchange fees in the EFTPOS system gained ACCC authorisation, but was subsequently overturned by the Australian Competition Tribunal. Further, some are concerned about the liability of directors of the ATM Access Company if the arrangements are found to constitute price fixing.

Even if the industry did decide to proceed with some aspects of the Access Code, the failure of the current Access Code to address interchange fees and connection costs would leave unresolved the central issues that have raised concerns over many years. Further, despite the technical changes to allow direct charging having already been put in place, a decision by the Bank not to impose an access regime would be likely to lead to some industry participants becoming reluctant to enter business arrangements with ATM owners that choose to direct charge.

If the reform package were to be abandoned, the cost and effort that has already been applied by the industry to ready itself for the implementation of the package will have been unnecessary. While this can be thought of as a sunk cost, the failure of these reforms would nevertheless likely lead to a presumption that genuine industry-based reform is not possible, at least under the current legislative framework. Given that there are many elements of the payments system

where further reform would be desirable, this would be an unfortunate outcome. It is therefore possible that limited regulatory intervention in the current case could help to head off the need for greater regulatory intervention in the future.

6.1 Conclusion

It is the Bank's view that the benefits of setting an access regime and thereby ensuring that the ATM reform package is implemented in its entirety outweigh the possible disadvantages and costs of imposing such a regime. In contrast to the alternative where the Bank does not regulate, it ensures that the reforms will be implemented with the associated public benefits. This is particularly true given that the industry costs of implementing the reforms have already been incurred by the participants.

7. Conclusion and Implementation

The final Access Regime for the ATM system is set out in the Attachment. It is largely unchanged from the draft Access Regime gazetted on 10 December 2008 with the exception that it explicitly prohibits charges for the establishment of direct clearing/settlement arrangements and provides the Bank with the option of exempting participants from some or all of the interchange provisions.

The Access Regime will be effective from 3 March 2009 and will complement the industry's ATM Access Code, which will also come into effect on 3 March 2009.

Attachment

Access Regime for the ATM System

Objective

The objective of this Access Regime is to promote competition and efficiency in the Australian payments system, having regard to:

- (i) the interests of current participants in the ATM system;*
- (ii) the interests of people who, in the future, may want access to the ATM system;*
- (iii) the public interest; and*
- (iv) the financial stability of the ATM system.*

Application

1. This Access Regime is imposed under Section 12 of the *Payment Systems (Regulation) Act 1998*.
2. This Access Regime applies to the payment system operated within Australia known as the ATM system, which was designated as a payment system on 10 December 2008 and referred to below as the ATM system.

3. In this Access Regime:

‘Access Provider’ has the same meaning as in the ATM Access Code;

‘Access Seeker’ has the same meaning as in the ATM Access Code;

‘APCA’ means the Australian Payments Clearing Association Limited (ABN 12 055 136 519);

‘APCA’s 2008 costs survey’ is the survey, conducted by APCA, of the estimated incremental direct costs to Access Providers of providing to an Access Seeker a Direct Connection Service or a Direct Clearing/Settlement Service, the final results of which were supplied to the Reserve Bank of Australia in November 2008;

an ‘ATM’ means an automatic teller machine in Australia;

an ‘ATM Acquirer’ has the same meaning as in the ATM Access Code;

‘ATM Access Code’ means the ATM Access Code adopted by ATM Access Australia Limited (ABN 53 130 571 103) on 23 February 2009 to commence on 3 March 2009, and as varied from time to time;

an ‘ATM Issuer’ has the same meaning as in the ATM Access Code;

an ‘ATM sub-network’ is a component of the ATM system for which access is provided on a multilateral basis, rather than by bilateral negotiation, and for which there is a common, multilateral interchange fee;

‘ATM transaction’ means a cash withdrawal, balance enquiry, or any other service obtained from an ATM in the ATM system in Australia;

‘Connection Agreement’ has the same meaning as in the ATM Access Code;

‘Connection Charge’ means the charge payable by an Access Seeker to an Access Provider under a Connection Agreement as described in Clause 3 of Schedule 3 of the ATM Access Code;

‘Direct Clearing/Settlement Service’ has the same meaning as in the ATM Access Code;

‘Direct Connection Service’ has the same meaning as in the ATM Access Code;

‘Direct Connector’ means a participant that exchanges ATM transaction messages, and clears and settles ATM transactions using two or more direct connections;

an ‘interchange fee’ is a wholesale fee which is payable by an ATM Issuer to an ATM Acquirer when a cardholder of the ATM Issuer undertakes an ATM transaction that is acquired by the ATM Acquirer;

a ‘one-way arrangement’ is an access arrangement whereby an ATM Issuer pays an interchange fee to an ATM Acquirer for use of an ATM by a cardholder, but that same ATM Acquirer does not pay an interchange fee to access any ATMs of the ATM Issuer in the arrangement;

terms defined in the *Payment Systems (Regulation) Act 1998* have the same meaning in this Access Regime.

4. Each participant in the ATM system must do all things necessary on its part to ensure compliance with this Access Regime.
5. If any part of this Access Regime is invalid, it is ineffective only to the extent of such part without invalidating the remaining parts of this Access Regime.
6. This Access Regime is to be interpreted:
 - in accordance with its objective; and
 - by looking beyond form to substance.
7. This Access Regime comes into force on 3 March 2009.

Price of access

Connection Charge for providing the Direct Connection Service

8. The Connection Charge levied by an Access Provider for providing the Direct Connection Service to an Access Seeker must not exceed the Direct Connection Cap, calculated in accordance with paragraph 9 below, applying on the date the Connection Agreement is entered into.
9. From 3 March 2009, the Direct Connection Cap for the Connection Charge in the ATM system is the lowest estimated cost for providing a Direct Connection Service as measured in APCA’s 2008 costs survey. This cost is \$76 700 (excluding GST).

Connection Charge for providing the Direct Clearing/Settlement Service

10. From 3 March 2009, no charge may be levied between participants in the ATM system for providing the Direct Clearing/Settlement Service.

Interchange fees

11. From 3 March 2009, no interchange fee shall be paid between participants in the ATM system in relation to any ATM transaction, unless the interchange fee is being paid by:

- (i) a participant with a one-way arrangement to access one, and only one, other participant's ATMs and the fee is paid in respect of this arrangement; or
- (ii) a participant that is a member of an ATM sub-network and the fee is the common interchange fee payable between the members of the sub-network, and the fee is paid to another member of that sub-network.

12. A participant that pays an interchange fee in a one-way arrangement cannot receive an interchange fee from any other participant in the ATM system unless both those participants are members of an ATM sub-network and the interchange fee is the common interchange fee payable between members of the sub-network.

Transparency

13. Each ATM Acquirer in the ATM system that receives an interchange fee within the terms of sub-paragraph 11(i) must report that arrangement to the Reserve Bank of Australia no later than 3 April 2009 for existing arrangements or within thirty days of the date the arrangement is entered into for new arrangements.

14. The administrator of an ATM sub-network or a representative of the participants in an ATM sub-network must publish the multilateral interchange fee of the sub-network on the administrator's website or on a representative of the participants' website, or make the multilateral interchange fee generally available through other means.

15. The administrator of an ATM sub-network must publish the rules that govern access to the sub-network.

Exemptions from paragraph 11 of this Regime

16. The Reserve Bank may grant an exemption to a participant in the ATM system from any or all of the requirements of paragraph 11 where it is satisfied that the exemption is appropriate, having regard to:

- (a) whether granting the exemption would be in the public interest;
- (b) the interests of current participants in the system;
- (c) the interests of people who, in the future, may want access to the system; and
- (d) any other matters the Reserve Bank considers relevant.

17. Where the Reserve Bank grants an exemption it will publish notice on its website that an exemption has been granted, the nature of the exemption and the identity of the participant(s) involved.