

13 August 2024

Retail Payment System

Recommendation to the Minister to
designate the interbank payment
network - August 2024



Recommendation

To: Hon Andrew Bayly, Minister of Commerce and Consumer Affairs

Date: 13 August 2024

Classification: In confidence

Subject: Recommendation to designate the interbank payment network under the Retail Payment System Act 2022

Purpose

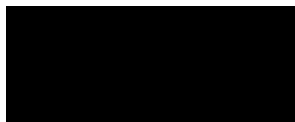
1. To recommend that you designate the interbank payment network as regulated under the Retail Payment System Act 2022.

Recommendations

2. The Commerce Commission recommends that you:
 - a. **Agree** to designate the interbank payment network under the Retail Payment System Act. *Agree / Disagree*
 - b. **Note** that this memo sets out a summary of the Commission's reasons for the recommendation to designate the interbank payment network. The Commission's full reasons are attached.
 - c. **Note** that designation will require an Order in Council to be passed which contains a designation order. To assist you in progressing this quickly should you wish to, we have provided a draft of the key contents for a designation order in our attached recommendation papers.
 - d. **Note** that the Commission's full reasons contain detail that can be incorporated in a Regulatory Impact Statement and material in support of a Designation Order.

Attachments

Statement of Reasons for recommending designation



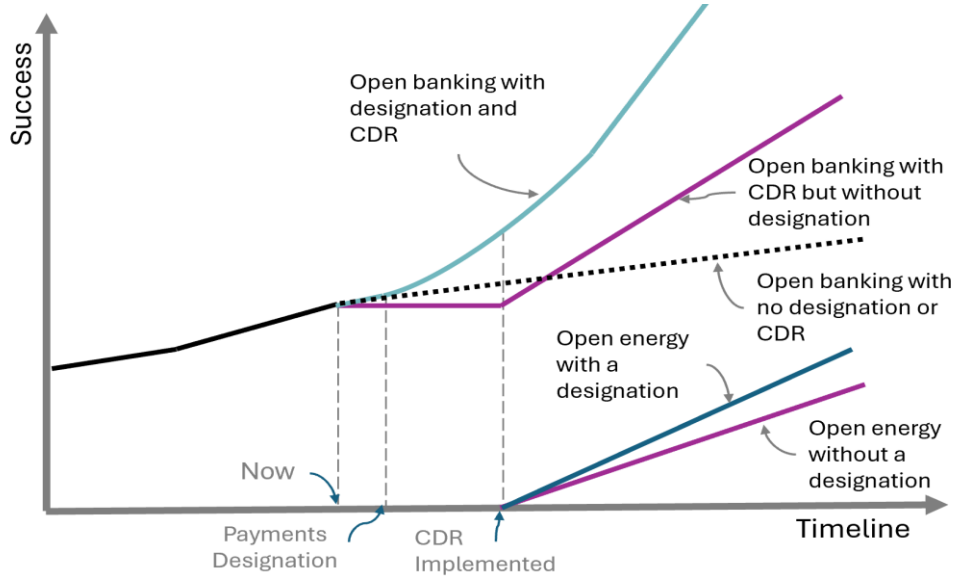
John Small
Chair

13 August 2024

Hon Andrew Bayly
Minister of Commerce and Consumer Affairs

Why we recommend designation

3. We recommend that you designate the interbank payment network under the Retail Payment System Act 2022 (the Act). Designation will reinforce the aims of the Customer and Product Data Bill (CPD Bill) by accelerating progress of open banking and reducing risk.
4. With designation of this network, we will actively drive competition and innovation in the retail payment system which is key to the success of open banking. This will enable the development and adoption of new, safe, low cost and accessible open banking payment solutions, including an updated Eftpos, or viable alternatives, to compete with Visa and Mastercard.
5. Progress on the delivery and adoption of open banking payment solutions has been slow and there are barriers that will continue to inhibit delivery and adoption. Designation is needed now to empower the Commission to remove those barriers and deliver better and faster open banking payments. This will complement and enhance the effectiveness of the Consumer Data Right (CDR) in banking/payments and allow MBIE to focus on the economy wide rollout of the CDR. A payments designation will also allow faster progress to be made on energy, as the next sector to be designated.
6. Speed and risk management are obviously crucial, but designation will also expand the scope of the banking CDR. For example, many payments innovators (including Eftpos or replacements) will need access to digital wallets on reasonable terms; designation will allow us to ensure that outcome.
7. We will continue to assist MBIE in developing the CDR by sharing feedback and intelligence gathered in our work. We anticipate that the Commission and MBIE will enter into a Memorandum of Understanding to agree our respective roles to avoid regulatory overlap.
8. More generally, for open banking to succeed, it will be important for a regulator to be actively engaged with the industry to set expectations, drive progress, and harness industry expertise. Designation will give us the ability to do all this because we can remove barriers as they appear.
9. The figure below illustrates the differences in the speed and success of open banking and economy-wide CDR delivery and adoption under different scenarios. We have included this figure to demonstrate, in a simple way, the additional benefits of designation.



10. Banks and some other industry participants generally question the merits of designation and suggest that industry can solve any issues itself. On the other hand, fintechs and merchant representatives welcome our involvement. They recognise the need for faster delivery and adoption of open banking and are sceptical about the commitment of banks to deliver in a timely way. Fintechs are ready to deliver these benefits of open banking to consumers and businesses, but they need rapid progress.

Open banking will provide better outcomes for consumers and businesses

11. Open banking has become increasingly prevalent overseas and the potential competition and economic benefits of open banking in New Zealand are significant and widely accepted. Done properly, open banking will lead to increased competition and innovation across the retail payment system, resulting in:
- 11.1 **Better payment options for consumers.** For example, one of our immediate objectives will be to enable low cost and viable alternatives (eg, an updated Eftpos or a replacement) that can compete with Visa and Mastercard schemes – online and in person, with payments made and accepted using the consumer and merchant’s device of choice.
- 11.2 **Better payment options for businesses.** For example, in the UK, Xero has seen rapid adoption of a solution that allows businesses to initiate payments from inside their accounting software. These options can improve productivity, efficiency and reduce the incidence of employee fraud and scams perpetuated against businesses.

Designation complements and enhances the CDR

12. The interbank payment network is the largest retail payment network in New Zealand and involves all bank transfers, eg, direct debits, and automatic payments

amongst other payment instruments. This is also the network in which fraud and scams that involve a bank transfer takes place.

13. Without designation of the interbank payment network and the attendant ability for the Commission to influence that network, the long-term success of open banking in New Zealand may well be reduced. That is because the full benefits of open banking cannot be achieved by the CDR alone.
14. Under the CDR regime, which is focussed on consumer and product data, the potential scope of payments regulation is limited to rules around initiation and pricing of payments. As the general competition and payments regulator, the Commission has a wider remit. Under a designation the Commission will be able to address barriers to open banking within the payment system, including participant conduct, governance, payment system wide pricing and adoption issues that cannot all be resolved under the CDR.
15. For example, we have heard from fintechs that barriers created by non-bank participants exist that may slow down or prevent the adoption of open banking. We agree, and have identified the barriers as including:
 - 15.1 The terms of access to digital wallets (such as Apple Pay), meaning services may cost more than they need to, or are limited in other ways.
 - 15.2 The terms imposed on merchants to accept new payment solutions.
 - 15.3 Merchant willingness to continue to accept sub-optimal payment methods because they are accepted by all banks.
 - 15.4 Consumer unwillingness to adopt alternative payment solutions to Visa or Mastercard because of the alternatives are unsafe or require sharing confidential information with third parties (eg, screen scraping).
16. Because these are payment system issues, the CDR will not be able to fully address them. The Commission as the competition and payment system regulator can address these issues through a designation and subsequent intervention, where required.
17. We also note that an open banking regime relying principally on one regime has had only limited success in Australia and the UK. New Zealand has an opportunity to take a different path, with the CDR regime and a retail payments designation complementing each other in delivering better open banking outcomes.
18. That is not to diminish the role of the CDR in open banking. The CDR is essential to the delivery of open banking as it will deliver the data sharing, account action (eg, open and closing of accounts) and access accreditation required for third parties to access and use customer and product data. However, payments are also a key element of open banking (as the Australians are finding), and the success of open banking will be determined by the delivery and adoption of open banking payments.

19. The diagram below illustrates how designation complements CDR to deliver better payment outcomes.

Key element	Non-payment account actions	Data	Payments including initiation, pricing and adoption
CDR	In scope of CPD Bill		Not covered by CDR
Recommended Designation	Not covered by designation		Covered by designation

Designation speeds up the delivery and adoption of open banking

20. Time is of the essence. Open banking is lagging in New Zealand. Fintechs are ready to go, and if open banking is not delivered soon, there is a real risk that those fintechs may fail or move to other markets. We have been told that as many as 12 fintechs have gone into hibernation or redirected their focus away from open banking in the last 12 months due, at least in part, to the delays in open banking delivery. We are also concerned that any further delay will undermine fintech investment in New Zealand.
21. Designation will enable us to speed up and improve the industry efforts to deliver open banking such that, in the short term, there is less risk to timely:
- 21.1 **delivery of the prerequisites of open banking**, such as APIs and partnering between third parties and banks on reasonable terms;
 - 21.2 **delivery of strong competition for the dominant international card schemes.** Eftpos is in decline. A much larger proportion of retail payments are now going through the card schemes, and the cost of maintaining the Eftpos network is increasing relative to the diminishing volume of transactions. Designation can aid the delivery of an updated Eftpos and/or alternatives to compete with the card schemes; and
 - 21.3 **adoption of open banking payment solutions** by consumers and merchants that are functional, low cost, safe and convenient.
22. To address the barriers to the timely delivery and adoption of open banking, we have the following steps in mind:
- 22.1 from now – continue to engage with Payments NZ via the API Centre, banks and fintech community on bottlenecks affecting delivery of the prerequisites of open banking;
 - 22.2 within one month – agree respective roles and responsibilities with MBIE, should a designation be supported;
 - 22.3 within two months – understand any required changes to governance arrangements (eg, possible creation of a governance steering group) and set a time frame for implementation; and

- 22.4 within six months – understand the work required for delivery of an updated Eftpos and/or alternatives to Eftpos to provide strong competition for the dominant international card schemes and establish a time frame for implementation.
23. Designation of the interbank payment network now is also complementary to the future delivery of the data sharing and access accreditation aspects of the CDR:
- 23.1 if designation is granted now, the CDR regime will trail designation by about 15 months. Designation enables the Commission to lay the foundation for the CDR by addressing current industry shortcomings, including with the API Centre and bank delivery, such that the Minister and MBIE can speed up the delivery of the CDR by confidently incorporating industry standards and practices that will have already been developed under the supervision of the Commission; and
- 23.2 when the CDR is introduced, the Commission's payments work will be well under way and MBIE can focus on the data sharing, account action and accreditation aspects of open banking, knowing that the payments regulator is dealing with the payments aspect.
24. Without a designation, we see a risk of a pause where industry slows progress pending the implementation of the CDR, which will further delay the delivery and adoption of open banking.

Designation enables MBIE to focus on CDR delivery in other sectors

25. Ongoing regulation of the open banking payments system will be resource intensive. The Commission is currently resourced to regulate this sector, MBIE is not. Designation reduces the need for ongoing intervention by MBIE.
26. Designation, and our subsequent focus on the delivery and adoption of open banking payment solutions on the interbank payment network, will therefore enable MBIE to move onto CDR implementation in other important sectors of the economy rather than spend its time and resources on regulating payments, which is within the Commission's remit. This co-operative regulatory model may well be a template to reduce regulatory duplication where the CDR is introduced in other sectors where there is also a sector regulator.

Designation enables the Commission to oversee industry

27. Industry input is essential to the successful delivery of open banking. Initial progress by banks in delivering open banking was sluggish. We have focussed on encouraging industry action, in the last year we have seen increased momentum, which we attribute largely to the perceived threat that a designation may be pending.
28. But there is still a long way to go. Designation allows us to continue to encourage those industry efforts, leveraging off the progress already made, while using our regulatory tools to assist or direct where appropriate, including by:

- 28.1 **influencing governance arrangements and the transparency of decision making** within Payments NZ Ltd and the API Centre and, if desirable, requiring change to those arrangements should that be necessary;
- 28.2 **speeding up fintech partnering with banks on reasonable terms.** There is an apparent lack of willingness by some banks to partner with third parties on reasonable terms (ANZ provided access to Worldline in 2022 and since then no new fintechs are using its APIs);
- 28.3 **facilitating co-ordinated industry solutions.** Co-ordinated conduct authorised by the Commission under a designation is exempt from liability under the Commerce Act. As retail payment system and competition regulator, we will be able to facilitate discussions necessary to implement open banking without participants worrying about whether those discussions breach the law;
- 28.4 **facilitating efforts to fight frauds and scams.** Most scams occur on the interbank payment network and many consumers use sub-optimal payment methods (including screen scraping) that require them to provide their bank user names and passwords to third parties. Designation accelerates the move to safer, more efficient payment methods and provides the Commission with the tools to support industry initiatives to fight fraud and scams; and
- 28.5 **regulating, through network standards and rules** where needed.

Designation enables us to take an enduring system wide perspective

- 29. Designation enables the Commission to encourage **ongoing competition and innovation** across the entire retail payment system through development of new products. We want open banking payments to thrive and compete with the Visa and Mastercard networks and be a viable alternative to Eftpos. This requires ensuring any price regulation across the system, including surcharging regulation, promotes this outcome.
- 30. Designation also enables us to facilitate the **future adoption of new products by consumers and merchants.** It is crucial to look at both sides of payments to ensure that open banking payments are a success and that barriers to merchant (payee) adoption can be addressed.

Recommended designation order for the interbank payment network

31. Below is our recommended designation order. Designation will require an Order in Council to be passed which contains a designation order. To assist you in progressing this quickly should you wish to, we explain the content of this recommended designation order in our attached reasons paper.

- 1) The retail payment network known as the interbank payment network of which—
 - a) the person known as Payments New Zealand Limited, or successor to that company, is a network operator;
 - b) the network rules include (without limitation) the rules (as updated from time to time) described as:
 - i) the BECS rules that relate to payment instruments, in relation to retail payments;
 - ii) the Payments NZ rules that relate to network participants of BECS, in relation to retail payments;
 - iii) the Payments NZ rules that relate to network participants of the API Centre, in relation to retail payments;
 - iv) the API Centre rules in relation to retail payments, including API standards and non-functional guidelines, frameworks, terms and conditions and policies;
 - c) the payment products include all BECS governed payment instruments, in relation to retail payments;
 - d) the participant classes include (without limitation):
 - i) Registered banks in NZ;
 - ii) Third party payment providers;
- 2) This designation order continues in force until its expiry date corresponding to 10 years after the date on which the order commences or until it is revoked or replaced, whichever occurs first.