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September 2024

By email: retailpaymentsystem@comcom.govt.nz

Consultation Paper: Retail Payment System - Costs to Businesses and Consumers of Card Payments in Aotearoa New Zealand

Kia ora

I am writing to you on behalf of TSB Bank Limited ('TSB'). We have prepared this in response to the questions asked by the Commerce Commission ('Commission') in its *"Retail Payment System: Costs to businesses and consumers of card payments in Aotearoa New Zealand: Consultation Paper."* Our focus is on Question 19 (see Appendix 1), relating to the impacts we foresee resulting from further material reduction in interchange fees. This is of particular significance to TSB's ability to compete, as a small domestic retail bank.

For your reference, TSB is a New Zealand owned bank, operating for more than 170 years, owned by Toi Foundation, a philanthropic trust, which invests our dividends in the Taranaki community. Our focus is on retail banking and home lending, and we also have a growing book supporting small to medium businesses. In respect of retail banking, we have approximately 2% of the market share, as the sixth largest bank in New Zealand. We believe small domestic banks play a vital role in the New Zealand banking market. We offer a viable alternative to larger overseas owned banks and therefore keep the market competitive for consumers. We also take our role in contributing to our community seriously, both directly and through our shareholder, and are committed to the overall success of New Zealand Inc.

Question 19 asks: *"Please provide any evidence of other impacts a material reduction in interchange fees for Mastercard and Visa could have on the New Zealand retail payment system."* We agree with the Commission's goals of promoting competition and efficiency across the retail payment system in Aotearoa for the benefit of those making and receiving payments (consumers and businesses). However, in our view, significant reductions in interchange fees, need to be further considered and balanced against the context that a significant volume of payments are run at a cost to banks, with no interchange revenue. Facilitating these payments is expensive for banks – with high costs associated to security, regulatory compliance, and meeting the demands of continual innovation. A reduction in interchange fees is likely to disproportionately impact the future prosperity of small banks and lessen future payments investment / innovation within New Zealand banking. This in turn, will adversely affect long-term customer outcomes and choice.

Aspects of this letter are confidential and commercially sensitive (and redacted accordingly). We ask that the Commission preserves the confidentiality of this information at all times. This includes with reference to section 9(2) of the Official Information Act 1982 (OIA). We also ask that TSB is notified of any request made to the Commission under the OIA for release of the information provided to it and that the Commission seeks TSB's views as to whether the information remains confidential at the time the response to such a request is considered.

Please contact [redacted] should you wish to discuss our response further.

Ngā mihi,

Helen Barrowcliffe

Head of Retail Banking Products, TSB

Appendix 1 – *Question 19: Please provide any evidence of other impacts a material reduction in interchange fees for Mastercard and Visa could have on the New Zealand retail payment system.*

Cost for Small Banks to Participate / in the New Zealand Payments System.

The retail payments system in Aotearoa is a complex, multifaceted ecosystem with many players across banks, regulators, payment providers, network providers and ATM / terminal providers. Maintaining a safe and stable payments environment (to process all consumer payments efficiently and securely) has a significant cost to a smaller, locally owned banks like TSB.

This is exacerbated in New Zealand (more-so than for similar banks overseas) due to the uniqueness of Aotearoa's payments ecosystem with a product like EFTPOS that has no transaction / processing fees for the merchant. [redacted] Whilst larger banks can spread the cost of compliance across a wider revenue and customer base, smaller issuers are disproportionately disadvantaged by any further interchange reductions, as we have fewer other sources of revenue to offset this and absorb cost. This then flows into our ability to continue supporting a mix of dual network cards (i.e., supporting both EFTPOS and Mastercard / Visa routed transactions, and the duplication of cost / resource and complexity associated with supporting multiple payment schemes).

Overall, we believe that further reducing interchange only on Mastercard and Visa product types, without taking other actions, will hinder the ability of small issuers (such as TSB) to compete. Changes to interchange should be considered alongside other options like reducing the maximum cost for merchant fees overall or setting caps on the interchange costs for overseas issued cards used within New Zealand.

[redacted] Whilst the transactions processed via EFTPOS are free to merchants, they incur a significant cost to the card issuer (the bank), with no revenue opportunity to offset this cost. [redacted] As a smaller issuer, we have found, both through a competitive and customer demand perspective, customers want products with the features that come as mandatory on a Visa / Mastercard - such as contactless payments, tokenisation to pay via Google and Apple devices, online shopping, and the ability to transact globally, alongside chargeback and fraud protections. Revenue is critical to our investment ability to build and maintain these features, and to innovate for the betterment of our customers. Where interchange is reduced, this demand for innovation and new features / protection from customers must be funded via higher fees (where permissible) and / or interest margins – resulting in either a net loss to customers for a benefit to businesses / merchants, or a reduction in competition / efficiency and innovation within the payments system (as we have already seen with EFTPOS).

Having the ability to self-fund transactions, through interchange is important for new players in the market and supports increased competition. We have seen this in Australia through neobanks like Up, Volt and Xinja which commonly take up a Mastercard or Visa debit card as their first product supporting a deposit account due to:

i. functionality - driven from the prior investments from Visa and Mastercard into enabling lower cost digital first propositions.
ii. simplicity and the ability for a wide number of players to easily participate in the scheme environment without requiring reciprocal, bilateral links like EFTPOS; and
iii. revenue via interchange, enabling them to continue growing and investing without having the significant compliance burden of participating in the payments ecosystem without the revenue associated with these transactions.

We hope that the above reasons will be considered as useful evidence as to the adverse effects on Aotearoa's retail payment system resulting from material reductions in interchange fees for Mastercard and Visa.