



NATIONAL AUSTRALIA BANK SUBMISSION

Australian Payments System Review

January 2021

Introduction

NAB welcomes the opportunity to provide a submission to the Payments System Review (Review). As a member of the Australian Banking Association (ABA) and the Australian Payments Network (AusPayNet), NAB has also contributed to their respective submissions to the Review.

Executive Summary

NAB supports the Government's desire to ensure the regulatory architecture of the Australian payments system is fit for purpose for a digital economy.

The payments ecosystem is a key enabler of important elements of Australia's sophisticated and emerging digital economy, including Data, Privacy, the Consumer Data Right (CDR), Digital Identity (Digital ID), central bank digital currency, communication and carriage services, Anti-Money Laundering and Counter-Terrorism Financing (AML-CTF) requirements, sanctions, competition, innovation and productivity.

A stable and sustainable payment ecosystem requires user confidence, resilience, trust and security. It also requires strong identification of payment initiators, assurance of payment receivers and robust exception and dispute handling to ensure consumer protection.

While these fundamental attributes remain relevant, the nature, information and integration of payments is changing as the economy digitises. Rather than being an action that occurs outside a purchase or provision of service (e.g. cheque and direct entry), or even at the end of a purchase decision (e.g. cards), payments are increasingly a transfer of value within a transfer of information or asset (e.g. in app purchases).

The current regulatory architecture has a prudential and stability focus, which has served Australia well over the past two decades. However, during this period:

- digital solutions increasingly allow consumers and merchants to choose from an array of payment methods to best meet their objectives;
- the payments system has become a far more significant component of the economy, driven by the growth in digital payment methods over physical payments methods such as cash and cheques;
- the principles-based regulatory approach has become more complex to respond to the evolving needs of Australia's modern economy; and
- the importance of payment system resilience has increased in order to ensure the continuous smooth running of the digital economy.

In the context of this changing landscape, the limitations of the current payments regulatory framework are exacerbated and include i) an assumption payments are stand alone and vertical in nature and initiated and concluded within a banking system context, and ii) limited agility to quickly respond in a co-ordinated way to emerging trends which impact the payments ecosystem (for example consumer choice routing, alternative stores of value, embedded payments, cyber risk, digital currency and Digital ID).

The key opportunity is to evolve the regulatory framework to ensure the Australian payments system remains fit for purpose. Greater clarity of accountability and strategic co-ordination across regulators, in particular ensuring empowerment to act across the entire payments value chain to address risks and opportunities, and the development of a national long-term strategic roadmap would be beneficial.

NAB considers that regulators must continue to have appropriate expertise and offer an objective view based on clear transparent objectives. Self-regulation should also continue to be an important part of the regulatory framework to support efficient innovation and customer focus across the ecosystem. NAB also considers that key regulators including the Reserve Bank of Australia (RBA), the Australian Competition and Consumer Commission (ACCC), Australian Prudential Regulation Authority (APRA), Australian Securities and Investment Commission (ASIC) and the Australian Transaction Reports and Analysis Centre (AUSTRAC) all have a critical role in the regulation of payments.

Updates to the existing framework to support clarity of accountability and the development of a long-term strategic roadmap would ensure greater consistency between regulators, maintain appropriate expertise while also giving effect to the Government's policy agenda. In particular it would support the Government's focus on driving an efficient digital economy, fostering competition and innovation, and maintaining privacy and consumer protection.

NAB recommends a holistic view of the payments value chain is taken in determining the most suitable approach, ensuring the proven positive attributes of the existing framework – such as principles-based regulation with specific reference to financial stability and prudential capacity – are maintained.

1. Does the regulatory architecture appropriately facilitate the development of an overall vision, strategy and principles for the Australian payments system?

The current co-regulatory architecture has to date shown capable of developing a clear vision and guiding principles for the Australian payments system and has proven successful in many critical areas, for example managing systemic risks that arise from change, driving efficiency and lowering costs for end users.

In addition, the Payments System Board (PSB), together with the Australian Payments Council (APC), has successfully executed on a strategic agenda for digital payments, fast payments, the payments mix, systemic resilience, financial crime and a Digital ID framework. This has been achieved within the context of privacy, access, promoting competition and innovation and achieving payments systems that are efficient and resilient.

However, as the Australian economy evolves to fully embrace digitisation and new technology emerges which enables payments innovation, NAB considers there is an opportunity for the regulatory architecture to also evolve to better facilitate the development of an overall vision and strategic roadmap for the payments ecosystem as a whole, along with clarity of accountability and co-ordination across regulating entities.

In NAB's experience, for example through its implementation of the CDR, it is critical for there to be a clear understanding and awareness of the roles, responsibilities and remits of regulating entities. Regulating entities should take an end to end view of the payments system and, regardless of whether it is accountable for all components, should share that perspective.

To clarify the roles and responsibilities of regulating entities, NAB recommends that as part of this Review, an independent party investigates and documents an end-to-end value chain map. This value chain of Australia's payments ecosystem could specify ownership, accountability, rules, regulatory oversight process and identify any current regulatory gaps or overlaps. The Review should ensure that whoever undertakes this mapping has the capability to do so and is not an existing participant or regulator in the system in order to provide an objective view.

2. How should our regulatory architecture be designed in order to balance the management of risk and efficiency in the payment system with the need for effectiveness for end-users?

Established participants in the payments system, such as major banks and large retailers, are typically subject to industry self-regulation and the mandates of formal independent regulators which, as set out in legislation, are primarily focused on stability, security, efficiency and low costs for end users.

The regulatory architecture, in terms of the specific bodies who are accountable for various elements of it, is best served by understanding the principles under which it operates, such as Swiss Financial Market Supervisory Authority's (FINMA) same risk, same rules approach, and the boundaries and remit of each body. This is necessary regardless of who regulates payments, because of how payments sit within ecosystems overseen by other regulatory frameworks. For instance, payments are digital, have privacy considerations, require security and identity protections, are reliant on carriage services, bolster financial markets and sit within a competitive environment.

The regulatory architecture should also consider the differing interests of end-users of the Australian payments systems being businesses, government and consumers. For example, an effective payments system for a consumer may be one with which they are able to make payments for goods and services quickly and for free, whereas for businesses or government the priority may be the ability to reduce fraud and operational expenses and manage working capital efficiently. In setting regulatory standards, the interests of one end user should not prevail consistently above the interests of another.

Risk, efficiency and effectiveness are all integral elements of payments systems and can vary depending on the use case. For instance, high volume payments prioritise efficiency and online payments seek frictionless interactions, whereas Delivery versus Payment (DvP) systems, which quarantine funds for settlement prior to transfer of an asset (e.g. share purchase or property settlement), may have higher risk and require more controls and less efficiency. Regulatory architecture should recognise the need for balance but be cautious in mandating an optimal balance.

Based on previous experience implementing major industry-wide initiatives (e.g. NPP and the CDR), NAB also considers a key objective in redesigning the regulatory architecture should be to avoid creating more process, structure and complexity. Instead, simplification should be prioritised along with clarity of both the design itself and the process undertaken to develop the design would also be beneficial.

The regulatory architecture should support the competitive landscape of the Australian payments system and recognise the need for commercial incentives for participants to pursue innovative and effective solutions for end-users. The initial private investment of established participants created the networks upon which all participants now rely, which has resulted in these participants having legacy systems to maintain and uplift to support innovation, security and efficiency for end users. New entrants to the Australian payments system, such as international schemes, fintechs, and Buy Now Pay Later (BNPL) schemes are not typically subject to the same self-regulation and independent regulatory standards. Unregulated or partially regulated participants can also drive innovation and effectiveness for some end-users at a higher price point. NAB believes new entrants need to fall under the remit of industry self-regulation to create a level playing field for all participants.

3. What is the appropriate balance between self-regulation, formal regulation and government policy to ensure the payment system continues to work in the best interests of end-users?

The current co-regulatory environment and balance between government policy, independent regulators and self-regulation has worked well to achieve positive outcomes for end users by promoting innovation, competition, public benefit, efficiency and resilience while enabling collaboration in areas which are not competitive.

The balance between self-regulation and formal regulation needs to be addressed to more widely encompass all participants in the Australian payments system and allow innovation and competition among all participants; both new entrants and existing. The number of independent regulators and the complexity of regulation could be simplified to make regulatory obligations more straightforward and streamlined. This would assist both new entrants and existing participants to have the required confidence and certainty to invest in and develop new forms of payment technologies which are tailored to the needs of end users.

4. Are there gaps (or duplication) in the current architecture that need addressing to ensure the system continues to work in the best interests of end-users?

As part of the growing digitisation of the economy, payments are increasingly becoming embedded in data information flows which are not necessarily for the sole purpose of payments, but are reliant on a payment to be completed, for example a property settlement. The current architecture assumes payments are a standalone vertical activity, rather than an enabler of other parts of the economy. It is not desirable to fragment payments regulation into other parts of the digital economy. The remit for payments should sit within payments regulatory bodies with a mechanism for interaction and review, and other regulatory bodies should seek to leverage payments regulation and capability.

As digitisation grows, gaps in regulatory remit and cross-functional permissioning to leverage existing frameworks have become more apparent. For instance, in exploring interoperability of Electronic Lodgement Network Operators where Registrars properly act at a state level, there was a risk that each state would determine or set a preferred payment method and architecture to effect property settlement, but payments regulators had no remit to ensure consistent and efficient use of payment architecture. The future regulatory architecture needs to have the ability to address these gaps and adapt to changing circumstances.

There are a number of developments in recent regulatory trends that have ensured proactive attention is given to supporting vulnerable customers and those at risk of financial hardship. It is recommended that when considering any changes to the existing architecture, these regulatory features should be maintained and applied across the payments ecosystem to all participants. These include:

1. Focus on problematic debt;
2. Focus on vulnerability and accessibility (for example through the Banking Code of Practice);
and
3. Abusive transaction prevention.

NAB has undertaken significant work on these areas and believes they have been beneficial for customers.

5. How should the regulatory architecture be designed to best facilitate the coordination of participants and regulators to meet the requirements of end-users?
6. What are the required features of a future regulatory architecture to ensure it is well-placed to meet the needs of end-users in relation to emerging innovations in the payments system such as those discussed above? Are changes needed to existing structures, roles and mandates involved in the governance of the system?

Regulatory architecture will need to be flexible enough to accommodate innovation that spans across multiple payment streams and avoid a siloed per-payment stream regulatory approach that may unnecessarily limit innovation.

Regulators need to take a holistic view of the system. The Inquiry into the Future Directions of the CDR has recommended that the CDR be expanded to permit payment initiation in the banking sector via a customer being able to authorise an accredited person to initiate a payment on their behalf. This has direct impact on many aspects of the payments system including fraud, security, liability frameworks and AML/CTF requirements.

Cross border payments by nature require consideration of global and inter-jurisdictional interests. While there are specific challenges to address, for example competing expectations regarding sanctions and anti-money laundering actions, the G20 is taking action through the Financial Stability Board and its Stage 3 roadmap for Enhancing Cross-Border Payments to meet these challenges.

Case Study: NAB StraightUp Card launch

The regulatory architecture should be structured to equally encourage innovation by incumbents as well as new entrants. For example, NAB launched a new product on 9 September 2020, the NAB StraightUp Card, a credit card that charges no interest for a monthly fee which is dependent on the selected credit limit (the monthly fee is reversed if the card is not used within a month). NAB's experience from launching this product was that the current regulatory framework can be slow to respond to innovative products, particularly offered by incumbents. NAB believes that the regulatory architecture for payments should allow regulators to respond efficiently to requests, particularly where the requests can demonstrate customer value and offer innovative digital banking products for consumers. Market participants would also benefit from greater transparency from regulators on the timeframes which will be followed for review of non-standard relief applications that apply to innovative products as applied in this example.

With the StraightUp Card product launch, NAB had a preference in product design to offer customers one of three credit limits (\$1000, \$2000, or \$3000). Unlike most credit cards, the minimum monthly repayment under the StraightUp Card is fixed based on the customer's credit limit rather than their statement closing balance.¹ The National Consumer Credit Protection Act requires that customers be allowed to apply for a credit limit decrease to any dollar amount within the product's credit limit range. NAB acknowledges the importance of this requirement as a way for consumers to manage their debt, however, found it more prescriptive when applied to a different type of product not necessarily envisioned by the requirement. The requirement meant that NAB now offers 16 different minimum monthly repayment amounts ranging from \$35 per month for a \$1000 credit limit to \$110 per month for

¹ See NAB information sheet available at <https://www.nab.com.au/content/dam/nabrwd/documents/guides/banking/key-facts-credit-cards.pdf>

a \$3,000 credit limit for the StraightUp Card.² It is an example of how application of prescriptive regulation can add complexity when the regulation is applied to newer or more innovative product types. More broadly, other prescriptive regulatory requirements designed for a more traditional credit card added complexity to the NAB Straight Up Card's product establishment, product documentation and how quickly the product could be made available to customers.

In the current architecture, not all market participants are subject to the same level of regulation. The future evolution of the regulatory architecture should seek to ensure there is consistency in regulation across participants in order to ensure an even standard of protection for consumers and merchants and so that regulatory principles around access, resilience and stability are broadly upheld.

Given the emerging growth in consumer usage and number of providers entering the market, the value chain review should also encompass the regulatory architecture for BNPL. In particular, consideration should be given to how payments are funded, whether that be via clear funds or the different forms of credit that will continue to emerge for both consumers and businesses.

In relation to Digital ID, which has broader use cases than just the CDR, the focus should be on creating a level playing field for competition through open standards rather than mandating specific standards or mechanisms. Defined mechanisms risk limiting innovation and acting as a commercial deterrent to building Digital ID capacities. The European Union's approach to Digital ID involves providing rules and principles but not mandating solutions or technology, thereby preferring open standards over defined mechanisms. Setting open standards would help to future-proof the CDR for emerging technologies. NAB encourages a consultative and integrated approach to developing open standards, which can then be leveraged for use under the CDR.³

7. What regulatory architecture is needed to provide support and clarity for businesses – particularly new entrants – to invest and innovate in our payments system?

Simplification of regulatory requirements to ensure they are more straightforward and streamlined will provide both new and existing participants in the payments system with the confidence and certainty to invest and develop new forms of payments technologies which are tailored to the needs of end-users. For example, AusPayNet's Navigating Payments for New Entrants, Participation and Licensing Summary shows anywhere between five and 10 licences and relationships are required for either direct or indirect access to Australian payments systems.⁴ There is an opportunity to consider streamlining requirements such as these.

8. How can the regulatory architecture enable participants in the payments system to make better use of data to improve cross-border payments and other payments that benefit end-users?

Regulatory architecture needs to be agile enough to rapidly assess any regulatory requirements for emerging technology and ensure consistency of end-user benefit in key areas such as privacy, security and customer protection. Architecture that segregates accountability or restricts the regulator from acting to fulfil their remit (e.g. on stability or competition) is not desirable. However, it also needs to enable participants to act individually or cooperatively to make improvements that benefit end users. For example, the RBA and APC were able to act cooperatively to assess the need for uplifting payment clearing systems to ISO20022 with the inclusion of sufficient and high-quality

² See information on NAB StraightUp Card Monthly Payments and Fees available at <https://www.nab.com.au/personal/credit-cards/nab-straightup-card/monthly-repayments-and-fee-info>

³ As noted in NAB's submission to the Inquiry into the Future Directions of the Consumer Data Right, May 2020.

⁴ See AusPayNet 'Summary requirements for participating in Australia's payments system' available at <http://auspaynet.com.au/resources/New-To-Payments-9>

information in payment messages, which will allow participants to implement effective monitoring, reporting and screening of payments to detect and prevent financial crime.

9. Given rapid changes to the system, what need is there for education for end-users (including consumers and businesses) about payments and who should provide that education?

The need for and extent of the education of end-users varies depending on the process or change, the parties involved and the outcome desired.

Business owners may require additional support and education on different payment options available to them, in particular understanding relevant costs and the management of risk in payments (such as minimising fraud, mistaken payments and credit risks). Providers of payments products should also provide accurate and simple to understand information to businesses and consumers. However, there could be a greater role for Government or other parties, including industry self-regulatory bodies, to supplement the information that payment providers offer customers on areas such as how the overall system operates and the features of different types of payment methods.

10. How does Australia's regulatory architecture compare with that of other jurisdictions, particularly as it relates to the encouragement of innovation and competition?

11. Are there any lessons from international experiences that can improve Australia's regulatory architecture to ensure it responds effectively to new developments in the future for the benefit of end-users?

NAB believes that payment regulators must continue to have appropriate expertise and offer an objective view. As an alternative to the Singapore and UK models, NAB suggests the model adopted by the Swiss Financial Market Supervisory Authority (FINMA) could be considered if there is a desire to more substantially change the regulatory architecture.

NAB supports the strong focus on innovation found in the New Zealand, Singapore and UK payments models as well as their recognition that regulatory focus on efficiency and low costs can at times encourage new entrants to remain outside of the direct remit of industry self-regulation and independent regulators. An example of this in Australia is the low number of new entrants which have taken advantage of the RBA's access regimes, due to the compliance obligations they would inherit from direct scheme membership. The more explicit relationship between the self-regulatory bodies in Singapore and the UK empowers self-regulators in their management of co-operation and collaboration between participants, which would be worth considering in the Australian context.

While there are benefits of considering New Zealand, Singapore and UK payments models, NAB also believes that there are other considerations such as the broader frameworks and systems in place in countries, funding models, expectations and history. NAB encourages the Review to consider the Swiss FINMA and Nordic payment systems, as good examples of systems which are principle-based and promote innovation. FINMA's principle-based regulation approach has encouraged innovation across the payments value chain, enabling innovation and compliance relatively quickly and cost effectively including integration of emerging technology and fintechs. The concept of same risks, same rules has also extended protection beyond just the immediately regulated financial sector. The Nordic payments systems have also shown that a regulatory environment that looks to facilitate innovation across a geographic area can achieve feasible

positive outcomes for end users.⁵ NAB acknowledges that the RBA has the power to regulate over a limited group.

Conclusion

A competitive and innovative financial services industry is critical to ensure good customer outcomes and growth of the economy more broadly. Ensuring that the regulatory architecture of the payment system is fit for purpose for a digital economy is one way of ensuring that the system continues to be able to support innovation that benefits customers and enhances the economy.

NAB looks forward to engaging further with the Review over the coming months and being of any assistance to the process.

⁵ The Nordic Payments Council is a common payments standard applied across Denmark, Finland, Sweden and Norway.