



21 July 2023

Director
Payments Licensing Unit
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

Dear Anna

Payments System Modernisation (Licensing: Defining Payment Functions)

Australia's payments system continues to see rapid innovation in both technology and business models with Australia's consumers amongst the fastest in the world to adopt new payments services offering convenience and enhanced customer experiences.

Security, consumer protection and the stability of the financial sector are essential components of the evolving payments ecosystem. Accordingly, the Australian Banking Association (ABA) welcomes the opportunity to provide feedback to the consultation paper, *Payments System Modernisation (Licensing: Defining Payment Functions)* which sets out to create a robust regulatory environment that promotes innovation while also ensuring the safety and security of the payments ecosystem. A licensing regime for payments providers with appropriate oversight and consumer safeguards should be implemented as a matter of priority to ensure that regulation evolves in line with industry innovation and provides adequate safeguards for consumers and payments ecosystem.

Participants in the payments system must adhere to the highest standards of transparency, accountability and risk management because of links between the payments system and the economy. This includes appropriate measures to addressing issues related to movement of scams and fraud proceeds and other forms of financial crime. With the advent of virtual currencies and decentralised finance, it is crucial to establish effective compliance measures that prevent illicit activities and promote a transparent financial ecosystem.

As the nation embraces the digital era, Australia must act swiftly to ensure that the payments system remains secure, resilient, and conducive to economic growth. Adequate regulation of new participants will be the cornerstone of achieving these objectives, safeguarding the interests of consumers, and bolstering the overall integrity of Australia's financial system by establishing minimum benchmarks that support consumer trust and regulatory confidence for all participants in the payments ecosystem.

ABA generally supports the types of payments functions proposed to be defined. ABA advocates for all entities performing defined payments functions to be required to hold a licence, rather than only entities that face the customer or face a retail customer. In principle, ABA agrees with the proposal for payments services to be regulated under the Australian Financial Services Licence (AFSL), subject to the comments and additional considerations, set out below. The AFSL regime applies to foreign entities that provide a financial service in Australia, and ABA considers this is, conceptually, an appropriate geographical nexus that can be applied to payments.

A summary of the ABA's early views on licence obligations and alignment with other legislation or areas of government policy are below. Responses to consultation questions are in the Appendix.



Licence obligations

- ABA proposes that more stringent 'baseline' obligations apply to payments licensees, in addition to the general AFSL obligations. Applying enhanced baseline obligations is appropriate to reflect the risks that payments service providers can introduce into the payments ecosystem. For example:
 - Third party payments initiation can create new vulnerabilities to scams and fraud where neither the third party service provider nor the customer's bank has end-to-end visibility of the transaction or the customer's transaction history, so that both may lose opportunities to identify indicators of scams or fraud.
 - As Australians increasingly move to digital payments, fraud or a cyber attack at a service provider can cause significant inconvenience or financial loss to end customers, and can also have an impact on the efficiency of a payments system.
 - Poorly governed stablecoins can introduce systemic risk.
- ABA asks Treasury to consider specific baseline obligations relating to capital adequacy and operational resilience – including cyber security, information security, business continuity management, outsourcing, resilience to scams and fraud. This approach would be consistent with other jurisdictions. The *Corporations Act 2001* already imposes specific obligations for licensees that provide specific financial services, and ASIC has issued guidance setting higher requirements for classes of licensees (for example, FX dealers, responsible entities, retail OTC derivative issuers). Data sharing and reporting also need to be considered.
- As part of the work on the payments licensing regime, ABA asks Treasury to consider the role of the ePayments Code in the licensing regime and the payments regulatory architecture. The payments licence should impose obligations and liability that reflect the more complex payments value chains where more than one entity may cause delay or loss to the end customer. This can be the case, for example, with third party payments initiation. If these obligations and potentially, liability, are to be imposed using the ePayments Code, it would require a review and significant revision of the Code before it is mandated.

Alignment with other legislation and policy areas

- Given the potential interplay between the PSRA, payments licensing (including the proposed mandatory ePayments Code), external dispute resolution, and the Government's scams policy including mandatory codes of conduct, ABA asks Treasury to clarify which regime(s) and instrument(s) will be used to set requirements or regulatory expectations for payments service providers.
- Payments licensees' obligations under the AML/CTF regime should be clarified. Licenses that provide services to end clients should be reporting entities in relation to those clients.
- ABA reiterates our request for Treasury to consider avoiding duplicative regulation under a payments licensing regime. Banks are already subject to the full range of obligations under the AFSL and additional obligations as proposed. This approach has reduced duplication between the AFSL and prudential regimes, and between prudential regulation and critical infrastructure regulation.

Drafting considerations

- In addition to Treasury's questions in chapter 2 and chapter 4, careful consideration would be required as to how payments functions are defined as new financial products or services, and the interaction between these new products and services with other definitions, exemptions, specific inclusions and exclusions in Chapter 7 of the *Corporations Act*.



Australian Banking Association

- Questions about the perimeter of payments functions and 'adjacent' functions or services would likely arise, regardless of whether these reforms are implemented under the AFSL or via a separate licence regime.

ABA would appreciate the opportunity to discuss these responses. Please contact Rhonda Luo on rhonda.luo@ausbanking.org.au or 0430 724 852 with any queries.

Yours sincerely

Chris Taylor
Chief of Policy



Appendix: responses to consultation questions

1. Are there any other principles that should be considered in developing the list of payment functions?

None.

The AFSL regime applies to foreign entities that provide a financial service in Australia, and ABA considers this is, conceptually, an appropriate geographical nexus that can be applied to payments.

2. Is the list of payment functions comprehensive, or should other functions be included?

No gaps identified. However, if the list is intended to be non-exhaustive and be able to respond to new and emerging payment functions, then it may not be appropriate for the functions to be referred to in primary legislation.

3. Should all payment functions be treated as financial products under the corporations legislation or should some be treated as a financial service?

In principle agree with the proposal to treat SVF as a financial product, akin to a bank account, and to treat payments facilitation services as a financial service. Under this approach, we seek clarity whether the financial product in relation to which the financial service or payment service is provided would be a non-cash payment facility.

4. Does the term 'payment stablecoins' accurately describe the types of stablecoins this paper seeks to capture for regulation or are there other terms that may be more appropriate?

Yes.

5. Does the proposed definition of 'payment stablecoins' adequately distinguish itself from other stablecoin arrangements?

The definition seems clear with two caveats.

- Query if the definition should specify that a payment stablecoin is one where the stablecoins are pegged 1:1 to a fiat currency, or whether the proposed definition is intended to apply to stablecoins that are described or marketed as pegged.
- Legislation will need to clearly distinguish between 'payment stablecoin' and tokenised (cash) deposits.

6. Is regulation as an SVF an appropriate framework for the regulation of payment stablecoin issuers? If not, why? What would be an appropriate alternative?

ABA agrees with applying SVF regulation to issuers of payment stablecoins.

7. Does the list of proposed payment functions adequately capture the range of payment services offered in Australia currently and into the future that should be regulated under a payments licensing regime?

Yes at present, noting the tension between allowing this list to evolve and specifying certain functions as a regulated financial service.

8. Does the list need to be broken down in more detail, for example, should facilitation, authentication, authorisation and processing be separate functions?

Not unless specific obligations need to apply to a particular function.

9. Should any other payment functions be included?



This list of payment functions seem to be sufficient to cover current businesses and anticipated businesses. Note case for maintaining flexibility in this definitions list.

10. Would the removal of the identified exclusions create unintended consequences?

11. Which existing exclusions and exemptions applicable to non-cash payment facilities should be amended or removed to support regulation of the proposed payment functions? Do any existing exclusions or exemptions require updating, such as the relief for low-value facilities?

Agree with the removal of the exclusions and exemptions for:

- Exchange and settlement between non-cash payment providers
- Certain electronic funds transfers
- Unlicensed product issuers that use licensed intermediaries

12. Should the incidental product exclusion apply to the proposed list of payment functions?

No. Most payments providers offer a range of services. An incidental products exclusion can create opportunity for regulatory arbitrage.

13. Should any exclusions or exemptions be revised to be more consistent with comparable jurisdictions? For example, should the 'single payee' exclusions and relief for loyalty schemes, electronic road toll devices, prepaid mobile phone account and gift cards be replaced by a general exclusion for payment instruments that can be used only in a limited way?

No, current exclusions seem to be appropriate. Given the ways in which payments can evolve, ABA does not support a general exclusion for payment instruments that can only be used in a limited way.

14. Should the exclusion for low value facilities apply to any PFS, such as money transfer services? If so, what thresholds should be considered a low value PFS?

No, low value should not form the ground for exclusion.

15. Should any other exclusions or exemptions be provided?

None identified.

16. Are there any other risk characteristics of a payment function that should be considered?

In principle, ABA agrees with the identified risks and makes further comments about the baseline regulatory obligations that may be necessary to address these risks.

ABA advocates for higher 'baseline' obligations to apply to all payments licensees. Applying enhanced baseline obligations is appropriate to reflect the risks that payments service providers can introduce into the payments ecosystem. For example:

- Third party payments initiation can create new vulnerabilities to scams and fraud where neither the third party service provider nor the customer's bank has end-to-end visibility of the transaction or the customer's transaction history, so that both may lose opportunities to identify indicators of scams or fraud.
- As Australians increasingly move to digital payments, fraud or a cyber attack at a service provider can cause significant inconvenience or financial loss to end customers, and can also have an impact on the efficiency of a payments system.

17. What are the types of payment risks posed by the performance of each of the proposed payment functions?



ABA is happy to discuss further with Treasury the risks that can be posed by proposed payments functions, but considers higher 'baseline' obligations should apply to all payments licensees to reflect the risks that payments service providers can introduce into the payments ecosystem. For example:

- Lack of adequate financial resources or capital is a risk for other payments functions, not just stored value facilities. A payments service provider can become insolvent and leave customers out of pocket for money 'in transit'. Customers can also be left out of pocket in case of insolvency if errors result in misdirected payments or weaknesses in controls create vulnerabilities to scams and fraud.
- Third party payments initiation can create new vulnerabilities to scams and fraud where neither the third party service provider nor the customer's bank has end-to-end visibility of the transaction or the customer's transaction history, so that both may lose opportunities to identify indicators of scams or fraud. Third party payments initiation also allows the layering of a payment with multiple participants in one transaction, which increases the risk of operational errors.
- As Australians increasingly move to digital payments, fraud or a cyber attack at a service provider can cause significant inconvenience or financial loss to end customers, and can also have an impact on the efficiency of a payments system.

18. While having regard to the obligations proposed to be imposed on the payment functions (outlined in Section 7), are the risks posed by the performance of each payment function appropriately mitigated by the payments licensing regime? Or are they more appropriately addressed by a framework outside of the payments licensing regime such as the PSRA or AML/CTF Act?

ABA reiterates our proposal relating to licensing obligations, particularly for higher 'baseline' obligations to apply to all payments licensees. Applying enhanced baseline obligations is appropriate to reflect the risks that payments service providers can introduce into the payments ecosystem. This includes capital adequacy requirements consistent with the EU and UK.

In relation to the PSRA and AML/CTF Act:

- While there is overlap between the regulatory remits of the RBA under PSRA, and ASIC under payment licensing, this overlap may be appropriate and can be resolved with regulator coordination. There is precedent for RBA and ASIC being co-regulators of clearing and settlement facilities.
- Payments licensees' obligations under the AML/CTF regime should be clarified. [Licenses that provide services to end clients should be reporting entities in relation to those clients.]

ABA highlights potential duplicative regulation for banks and proposes that banks should be taken to comply with relevant payment licensing obligations where the bank is subject to prudential regulation.

19. Is the proposed risk-based approach to applying regulatory obligations appropriate?

ABA reiterates our proposal relating to licensing obligations, particularly for higher 'baseline' obligations to apply to all payments licensees. Applying enhanced baseline obligations is appropriate to reflect the risks that payments service providers can introduce into the payments ecosystem.

ABA agrees in principle that licensees that seek to have direct access to a payments system should be subject to specific obligations and potentially enhanced ongoing oversight. As payment systems develop, some may not have a clear distinction between direct, indirect and other types of participants. There may be a case to retain sufficient flexibility in the licensing regime so that appropriate obligations may be scaled and applied to payments service providers in such systems, even if they do not perform a clearing and settlement role.



20. Should payment functions that are not customer facing be required to hold a payments licence? Should providers of these non-customer facing payment functions have different regulatory obligations, such as only having to comply with relevant industry standards?

Yes, these service providers should still hold a licence. Other than ABA's comments about higher or additional licence obligations we believe the AFSL regime can apply as is.

For example, if an entity does not have a customer facing role, the entity would not be required to provide disclosure documents in relation to the regulated financial product or service. If the entity only provides payment services to wholesale clients, then the AFSL regime already provides for relief from a number of licence obligations. Licensing is still required to ensure the provider is still subject to other licence obligations, because their action or inaction can still cause harm or disrupt a payments service.

21. Should the common access requirements and industry standards be linked to the payments licence? For example, would it be appropriate for some entities to only be required to comply with mandatory industry standards but not be required to hold an AFSL or comply with the ePayments code?

Common access requirements should be linked to the payments licence, and the licence should provide for robust and ongoing oversight of licensees that rely on the payments licence to become a direct participant in a payment system.

In general, compliance with payments industry standards should be linked to the payments licence and be an obligation of holding such licence.

Compliance with the ePayments Code may depend on the nature of payment services provided and/or the type of clients. It would also depend on the content and scope of the revised, mandatory ePayments Code. The ePayments Code needs to be revised to set out customer liability as between PSPs along a payments value chain for (for example) unauthorised payments. It follows both customer facing and non-customer facing PSPs need to be required to comply with relevant parts of the Code.

22. What types of businesses should be subject to the common access requirements? There is limited information available on the number and size of non-bank PSPs interested in directly participating in Australian payment systems to clear and settle payments. If this is something that your business is interested in, please provide further information (including via a confidential submission).

All non-ADIs that seek to gain access to payment systems as direct participants should be required to comply with the common access requirements.

23. Further information is sought to help identify the number and profile of participants that perform each payment function and therefore may potentially be affected by the new licensing framework.

24. How can the payments licensing processes across regulators be further streamlined?

ABA highlights potential duplicative regulation for banks and proposes that banks should be taken to comply with relevant payment licensing obligations where the bank is subject to prudential regulation. This approach would help to streamline payments regulation across APRA and ASIC.

25. Is the proposal to provide central guidance and a website portal for PSP licensing processes a good alternative to the single point of contact proposal recommended by the Payments System Review?

A more substantive issue would be alignment and removal of duplication between regulatory regimes. If there is inconsistency between regulatory regimes, the existence of a central source of regulatory guidance may have limited impact on reducing unnecessary regulatory impost.