

SUBMISSION

PAYMENTS SYSTEM MODERNISATION

JULY 2023

INTRODUCTION

The Australian Retailers Association (ARA) welcomes the opportunity to provide a submission to Treasury regarding the proposed Payments System Modernisation (Licensing: Defining Payment Functions).

The ARA is Australia's oldest, largest and most diverse retail body, representing a \$400 billion sector that employs 1.3 million Australians. As Australia's peak retail body, the ARA informs, advocates, educates, protects and unifies our independent, national and international retail members trading through online stores and more than 120,000 retail shop fronts across the country.

The payments ecosystem is of critical importance to the retail sector, and retail transactions form the core of Australia's payments system.

Retailers are continually adapting to rapid technological changes, the emergence of new business models, and evolving customer behaviours. However, the increasing complexity of the payment's ecosystem poses challenges for both consumers and retailers in terms of efficiency, reliability, and cost management, given the expanding array of payment options available.

In response to this dynamic environment, the ARA recognises the significance of these reforms in shaping the future of the payments landscape and ensuring a robust regulatory framework that supports innovation, consumer protection, and competition.

The ARA also acknowledges the scope of the proposed reforms, which include defining payment functions and establishing a licensing framework for payment service providers (PSPs). We understand that the intention is to modernise the regulatory framework to better align with emerging payment technologies and business models, while also addressing potential risks and ensuring appropriate consumer safeguards.

As a peak body representing the retail industry, we emphasise the importance of a collaborative and consultative approach in the development and implementation of these reforms. The retail sector plays a critical role in the payments ecosystem, and it is essential that the views and concerns of retailers are thoroughly considered to create a regulatory framework that is practical, effective, and supportive of their needs.

EXECUTIVE SUMMARY

The ARA has reviewed the proposed legislative reforms outlined in the Treasury's Discussion Paper on Payments System Modernisation. The ARA acknowledges the importance of modernising the payments system to meet the evolving needs of the retail industry and consumers. Based on consultations with our retail members, we have formulated a position that addresses key concerns and provides recommendations for effective and balanced regulatory measures.

1. **Principles:** The ARA advocates for the consideration of key principles in developing the list of payment functions. These principles include continuity and reliability, quality assurance, secure data sharing, agility and adaptability, comprehensive consumer protection, and harmonisation with global standards. By incorporating these principles, the regulatory framework can promote a well-functioning payment system that supports retailers and ensures a seamless customer experience.
2. **Payment Functions:** The ARA recommends that the final list of payment functions be communicated clearly and unambiguously to all parties affected by the proposed reforms. This clarity is crucial to prevent misunderstandings and non-compliance. In determining the full scope of payment functions, we suggest the inclusion of higher risk support functions that impact the core payment value chain, such as security, fraud prevention, and privacy.
3. **Classification of Payment Functions:** the ARA recommends that payment functions be classified as 'payment functions' without the need for a lower-order categorisation as products or services. This approach allows for a more inclusive and adaptable regulatory framework, supporting the growth, innovation, and sustainability of the retail industry and the broader payments ecosystem.
4. **Payment Stablecoins:** The ARA acknowledges the term 'payment stablecoins' as an accurate description of the types of stablecoins this paper seeks to regulate. However, we recommend further clarity on the definition of payment stablecoins, specifically regarding stablecoin definition intent and purpose in the context of the proposed legislation.
5. **Regulatory Framework:** The ARA supports the regulation of payment stablecoin issuers under the framework of Stored Value Facilities (SVF). We believe this regulatory framework appropriately addresses the risks associated with payment stablecoins while providing a clear and effective oversight mechanism.
6. **Comprehensive Coverage:** The ARA affirms that the proposed list of payment functions adequately captures the range of payment services currently offered in Australia. We recommend extended consultation with industry stakeholders to test those functions for comprehensive coverage and avoid unintended gaps or inconsistencies.
7. **Detailed Clarity:** The ARA emphasises the need for detailed clarity in the list of payment functions. Further breakdown of functions, such as facilitation, authentication, authorisation, and processing, may be necessary to provide specific guidance and avoid ambiguity in compliance.
8. **Risk Considerations:** The ARA highlights various risk characteristics associated with payment functions. These include acceptance and adoption risk, integration risk, fraud and chargeback risk, payment disputes, transaction processing risk, transaction reversal risk, operational risk, security and fraud risk, systemic risk, and compliance and regulatory risk. It is essential to consider these risks and ensure appropriate mitigation measures within the payments licensing regime or relevant frameworks.

The ARA's position aims to strike a balance between regulatory requirements and operational feasibility, while fostering innovation and competition, protecting consumer interests, and providing clarity and certainty for retailers navigating the evolving payment landscape. These recommendations reflect the ARA's commitment to supporting a modern, efficient, and secure payments system that benefits both retailers and consumers.

RESPONSE AND RATIONALE

The following considerations outline the ARA's rationale for these recommendations and detailed responses to the questions raised in the Treasury's Discussion Paper.

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

- a. **Continuity and Reliability:** Retailers require assurance that service providers will maintain their ability to offer payment services consistently and reliably. We need confidence that these providers will support our payment needs for the long term, ensuring smooth operations and uninterrupted customer experiences.
 - b. **Quality Assurance:** To uphold high standards in service delivery, retailers seek a robust quality assurance framework. It is essential that service providers meet minimum standards to ensure reliable and efficient payment processing. This will enhance customer satisfaction and protect retailers from potential disruptions or subpar services.
 - c. **Secure Data Sharing:** In today's digital landscape, the secure sharing of data is of utmost importance. The retail industry relies on payment systems that prioritise data security and protect sensitive information. We need assurances that proper measures are in place to safeguard customer data and maintain the integrity of transactions.
 - d. **Agility and Adaptability:** Retailers operate in a rapidly evolving payment landscape where new forms of payment emerge regularly. To stay competitive, we require a regulatory framework that fosters pace, flexibility, and easy-to-understand standards. This will enable us to adopt and integrate new payment forms seamlessly while meeting regulatory requirements.
 - e. **Comprehensive Consumer Protection:** The retail industry values consumer trust and advocates for adequate protections for our customers. We support regulations that safeguard consumer rights, ensure fair practices, and promote transparency in payment transactions. These measures will build confidence among consumers and foster a secure and trustworthy payment environment.
 - f. **Harmonisation with Global Standards:** To encourage innovation and attract international players, it is essential to align Australian regulations with established international standards. Striking the right balance between local requirements and global practices will promote a level playing field, encourage competition, and facilitate the entry of new overseas market participants.
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Is the list of payment functions comprehensive, or should other functions be included?

The list of payment functions captured in the consultation paper represent the core value chain of the payment system. Consideration might be given to higher risk support functions that impact the core value chain, for example security, fraud prevention and privacy.

Functions to be included should be communicated clearly and unambiguously to all parties affected by the proposed reforms. Clear communication is essential to prevent misunderstandings and misinterpretations that could lead to non-compliance or unnecessary burdens on business.

Should all payment functions be treated as financial products under the corporation's legislation or should some be treated as a financial service?

The ARA holds the view that classifying payment functions as either products or services may be counterproductive and unnecessarily restrictive. The distinction between products and services may not accurately capture the evolving nature of payment functions and the increasing convergence of product-based features and service-based functionalities within modern payment systems.

By categorising payment functions solely as 'payment functions' without the need for further lower-order definitions, a more inclusive and adaptable approach can be adopted. This broader categorization acknowledges the diverse range of activities and offerings within the payment's ecosystem, encompassing processing, facilitation, risk management, and other related functions.

Eliminating the rigid product-service divide allows for a regulatory framework that can better accommodate the complexities and nuances of payment functions.

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

A separate framework governing payment functions and their definitions would be appropriate. We would recommend extended consultation in developing such a framework.

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

- a. Issuance of Payment Stablecoins (Payment Stablecoin SVFs):
 - i. Acceptance and Adoption Risk: The retail industry may face challenges in accepting payment stablecoins as a form of payment due to concerns about stability, merchant acceptance, and customer adoption.
 - ii. Integration Risk: Retailers may encounter difficulties integrating payment stablecoin systems into their existing payment infrastructure, including point-of-sale systems and backend operations.

- b. Issuance of Payment Instruments:
 - i. Fraud and Chargeback Risk: The retail industry is exposed to risks related to payment instrument fraud, including unauthorised use, counterfeit instruments, and chargebacks, which can result in financial losses for merchants.
 - ii. Payment Disputes and Customer Disputes: Disputes arising from payment instruments, such as disputed transactions or customer complaints, can lead to additional administrative efforts and potential reputational risks for retailers.
- c. Payment Initiation Services:
 - i. Transaction Reversal Risk: Retailers may face risks related to transaction reversals initiated through payment initiation services, leading to inventory management challenges, reconciliation issues, and potential losses.
- d. Payment Facilitation, Authentication, Authorisation, and Processing Services:
 - i. Operational Risk: Service disruptions, system failures, or errors in payment processing can lead to delays, errors, or financial losses for customers and merchants.
 - ii. Security and Fraud Risk: Payment facilitation services may face risks associated with fraud, unauthorized unauthorised access, data breaches, and cyber-attacks that can compromise the integrity and security of payment transactions.
- e. Payments Clearing and Settlement Services:
 - i. Systemic Risk: Clearing and settlement services involve the finalization of payment transactions and the transfer of funds between financial institutions. Systemic risks include liquidity risks, settlement failures, and operational disruptions that can impact the stability and efficiency of the overall payments system.
- f. Money Transfer Services:
 - i. Compliance and Regulatory Risk: Money transfer services are subject to regulatory requirements, including anti-money laundering (AML) and counter-terrorism financing (CTF) regulations. Failure to comply with these regulations can lead to legal and reputational risks.

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*?

Due to the scope and complexity of the defined payment functions, a framework outside of the payments licensing regime would be appropriate.

SUMMARY OF RECOMMENDATIONS

Based on our assessment and the interests of Australian retailers, we make the following recommendations.

1. Principles	<ul style="list-style-type: none"> • Continuity and reliability, • Quality assurance, • Secure data sharing, • Agility and adaptability, • Comprehensive consumer protection, and • Harmonisation with global standards.
2. Payment Functions	<ul style="list-style-type: none"> • The final list of payment functions be communicated clearly and unambiguously to all parties affected by the proposed reforms. • Inclusion of 'higher risk' support functions that impact the core payment value chain.
3. Classification of Payment Functions	<ul style="list-style-type: none"> • Payment functions should be classified as 'payment functions' without the need for a lower-order categorisation as products or services.
4. Payment Stablecoins	<ul style="list-style-type: none"> • Further clarity is required on the definition of payment stablecoins, specifically regarding definition 'intent and purpose' in the context of the proposed legislation.
5. Regulatory Framework	<ul style="list-style-type: none"> • The ARA supports the regulation of payment stablecoin issuers under the framework of SVF.
6. Comprehensive Coverage	<ul style="list-style-type: none"> • The proposed list of payment functions adequately captures the range of payment services currently offered in Australia. • Extend consultation with industry stakeholders to test those functions for comprehensive coverage.
7. Detailed Clarity	<ul style="list-style-type: none"> • The final list of payment functions should have detailed clarity of definition.
8. Risk Considerations	<ul style="list-style-type: none"> • The ARA highlights retail industry specific risks, which require mitigation measures within the payments licensing regime and relevant frameworks.

These recommendations aim to enhance the proposed amendments, promote transparency, accountability, and effective regulation, and ensure the retail payments sector in Australia remains competitive, innovative, and customer-centric.

We trust that our response provides valuable insights from the perspective of the Australian retail sector. We remain committed to engaging in further discussions and collaborating with relevant stakeholders to shape a robust and forward-thinking regulatory framework for the payments industry.

Thank you for considering our input. We look forward to the opportunity for further engagement on this important matter. For any queries in relation to this submission please contact policy@retail.org.au

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