



COVERSHEET

Minister	Hon Dr David Clark	Portfolio	Commerce and Consumer Affairs
Title of Cabinet paper	Regulation of the Retail Payments System Additional Policy Approvals	Date to be published	8 September 2021

List of documents that have been proactively released		
Date	Title	Author
29 June 2021	<i>Regulation of the Retail Payments System Additional Policy Approvals</i>	<i>Office of the Minister of Commerce and Consumer Affairs</i>
30 June 2021	<i>Regulation of the Retail Payments System: Additional Policy Approvals Cabinet Minutes</i>	<i>Cabinet Office</i>
23 June 2021	<i>Regulatory Impact Statement: Additional tools for regulating the retail payments system</i>	<i>MBIE</i>

Information redacted

YES

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Some information has been withheld for the reason of Confidential advice to Government.

In Confidence

Office of the Minister of Commerce and Consumer Affairs

Chair, Cabinet Economic Development Committee

REGULATION OF THE RETAIL PAYMENTS SYSTEM: ADDITIONAL POLICY APPROVALS

Proposal

- 1 This paper seeks agreement to additional policy proposals for the regulation of the retail payments system. These include the method of designating parties for regulation, additional regulatory tools and enforcement powers for the Commerce Commission as the regulator.

Relation to government priorities

- 2 The Government committed to reducing merchant service fees (**MSF**) in the Speech from the Throne. The Government's intention is to bring these fees in line with overseas jurisdictions to reduce the burden on small businesses and the effect of these costs on consumers.

Executive Summary

- 3 New Zealand merchants continue to pay more than their Australian counterparts for accepting credit cards and online debit cards. This is due, at least in part, to an apparent lack of efficient competition in some aspects of the retail payments system. To address this, Cabinet agreed to set up a regulatory regime for the retail payments system, with the Commerce Commission (**the Commission**) as the regulator [DEV-21-MIN-0075 refers].
- 4 The regulatory regime defines the retail payments system in a broad sense, and sets out the criteria and process to determine which retail payment networks are designated for regulation. I am reporting back to Cabinet on the design of the designation process and other secondary policy issues.
- 5 I propose that the Minister of Commerce and Consumer Affairs, in accordance with a recommendation from the Commission, should recommend that retail payment networks be designated by Order in Council. The Commission will have the ability to issue standards that may cover pricing, access and information disclosure arrangements, and may issue directions around network rules. Before exercising these powers, the Commission will need to take into account criteria specified in the legislation. To ensure regulated parties comply, the legislation will include a civil enforcement regime that broadly aligns with the Commerce Act 1986.
- 6 Following Cabinet agreement, I will issue drafting instructions to the Parliamentary Counsel Office, with the aim of having a Retail Payments System Bill ready to introduce to the House. Confidential advice to Government I am seeking Cabinet's agreement to delegate

decisions to me on minor and technical matters that arise during the course of drafting.

Background

- 7 Retail payments provide for the transfer of funds from consumers to merchants for goods and services acquired. The retail payments system is constantly evolving and comprises of various retail payment methods like card products, cheques, cash, bank transfers and more recently, Buy-Now Pay-Later products.
- 8 MSF are fees payable by merchants to their acquirer, normally the merchant's bank. These relate to certain types of card payments, including credit or debit cards, whether they involve a swipe, contactless or online payment. Unlike many overseas jurisdictions, EFTPOS card transactions and debit card transactions that are not contactless or involve online payment, which currently make up roughly half of all card transactions, do not incur MSF in New Zealand.
- 9 While there have been moves in the past year to reduce fees, and the average MSF payable by New Zealand merchants for card products overall is comparable with Australia, New Zealand merchants continue to pay more for accepting credit cards and online debit cards. MSF for some card products in New Zealand remains high due to an apparent lack of efficient competition in some aspects of the retail payments system.
- 10 In April 2021, Cabinet agreed to set up a regulatory regime for the retail payments system, with the Commission as the regulator [DEV-21-MIN-0075 refers]. Cabinet agreed to:
 - 10.1. introduce a regime to regulate (on a case-by-case basis) classes of retail payments system participants, their providers and any associated infrastructure operators (including secondary infrastructures) to reduce economic inefficiencies in the retail payments system;
 - 10.2. establish a transitional price path to reduce interchange fees for the main credit and debit card schemes;
 - 10.3. appoint the Commission as the regulator;
 - 10.4. empower the regulator to impose pricing principles or limits on fees;
 - 10.5. in-principle decisions to empower the regulator to:
 - 10.5.1. impose information disclosure requirements;
 - 10.5.2. make directions to amend rules and systems; and
 - 10.5.3. accept enforceable undertakings.
- 11 Cabinet invited me to report back to seek further policy decisions on the following:
 - 11.1. institutional arrangements for coordination between the various regulators of payment systems;

- 11.2. the criteria and process for designation to be included in legislation;
- 11.3. the nature and scope of the tools available to the regulator;
- 11.4. an enforcement regime; and
- 11.5. commencement dates.

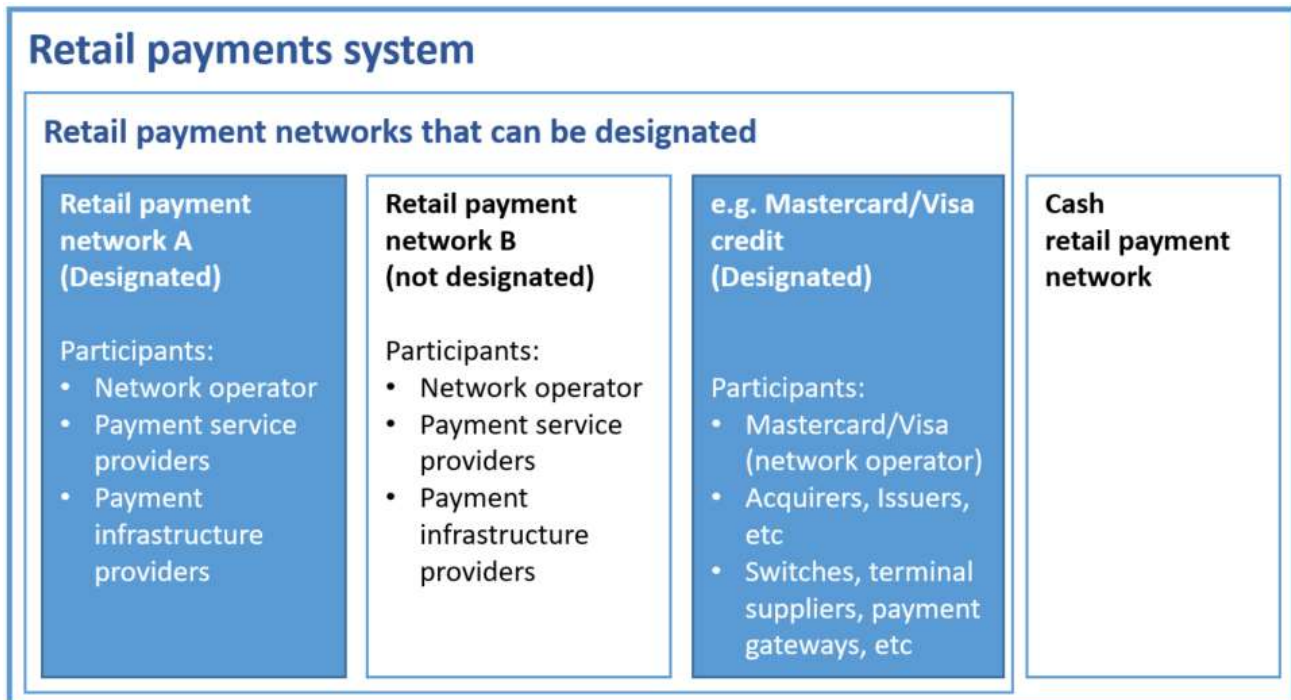
Objectives of the regime

- 12 Cabinet earlier agreed to an overall objective of the regime which was to ensure that the retail payments system delivers long-term benefits to merchants and consumers. This objective was supported by four aims:
 - 12.1. enable efficient competition between payment providers and payment products;
 - 12.2. incentivise beneficial innovation for consumers and merchants;
 - 12.3. be efficient in allocating resources through clear price signals, where prices are cost reflective for the system as a whole; and
 - 12.4. be fair in its distribution of costs, particularly in its treatment of small merchants and low income domestic consumers.
- 13 Drawing on these aims I consider that the objectives should focus primarily on retail payment networks being efficient and competition in the supply of retail payment services. Issues related to fairness and transparency should be secondary principles to which the decision-maker should have regard when considering the objectives.
- 14 This will create a clear hierarchy in objectives, which I consider will:
 - 14.1. be targeted at the regulatory problems which lead to high MSF for merchants and consumers;
 - 14.2. open a path to having fairness and transparency considered in the retail payments system once any concerns with efficiency and competition have been addressed;
 - 14.3. build on the competition and efficiency expertise of the Commission; and
 - 14.4. reduce the risk of legal challenge of the regulator's actions due to primary objectives having an already established legal basis.

Criteria and process for designation

- 15 Cabinet agreed to establish a regulatory regime based on a designation model, whereby the primary legislation would define the retail payments system in a broad sense, and set out the criteria and process for designation.
- 16 To provide greater clarity, I propose that the legislation allows for the designation of a retail payment network (**RPN**). In doing so, the legislation will be able to distinguish

between RPNs (a subset) and the retail payments system. The following figure provides a stylised example of the retail payments system:



- 17 The RPN captures all the participants operating in a RPN, which, in the course of business, enables the transfer of funds within the RPN. All payment instruments within each RPN are captured. For example the Mastercard/Visa credit RPNs include not just physical cards but also any payment instrument including tokenised credentials such as virtual cards, including methods like Apple Pay and Google Pay. Reference to RPNs will ensure the designation applies more broadly, without targeting just the specific entity that is operating or maintaining the RPN. This distinction will provide for dynamism of RPNs and allow the regulator to target the parts of designated RPNs that are causing issues.
- 18 The Bill will define retail payments system ‘participants’ to include payment service providers, infrastructure providers and network operators integral to the operation of a RPN.
- 19 I am proposing that the Minister of Commerce and Consumer Affairs should be responsible for recommending the designation of RPNs to the Governor General, through an Order in Council, on a recommendation from the Commission. In receiving the Commission’s recommendation, the Minister can only accept, reject or request the Commission to reconsider any matter (i.e. an error, oversight or competing policy interests).
- 20 In order to provide greater clarity and transparency for regulated parties, the designation may include detail such as:
 - 20.1. the payment products in the RPN;
 - 20.2. classes of participants, including those deemed to be critical to the operation of the RPN; and

- 20.3. the scope of rules that apply to the RPN.
- 21 In providing a recommendation regarding designation, the Commission must consider whether designation of the RPN is likely to promote the objectives of the regime, taking into account:
- 21.1. any features or conduct of the RPN that reduces or is likely to reduce competition or efficiency in the supply of retail payment services;
 - 21.2. the nature of the RPN being designated which includes consideration of:
 - 21.2.1. the number and value of the transactions that the RPN presently processes or is likely to process in the future; and
 - 21.2.2. the type of transactions that the system presently processes or is likely to process in the future.
- 22 The Commission must have regard to other regulatory requirements applying to the RPN.
- 23 The proposed criteria sets a high threshold for designation but seeks to provide an objective process that produces predictable and consistent outcomes across time and across the system. I consider the threshold for designation should be sufficiently high to ensure only those RPNs that have or are likely to have a genuine adverse impact on outcomes for merchants and/or consumers may be designated. This may be RPNs that are mature networks, or networks that are likely to grow and become mature quickly.
- 24 Before the Minister makes a recommendation, there should also be a requirement for the Commission to consult affected parties and publish the rationale for designation.
- 25 I did consider whether the decision to designate a RPN should instead be made by the Commission itself, given that consideration of the criteria involves detailed technical expertise. The Legislation Design and Advisory Committee emphasised that the decision to designate is a highly technical one and the Commission would have the expertise to assess the merits of designations. However, given the significant impact designation would have on regulated parties, I concluded that designations should have ministerial oversight. This ensures that the decision to designate takes into account both technical and wider policy issues. It also extends accountability beyond the Commission, which is particularly important as it avoids the Commission having to decide on whether to regulate, the form of regulation to be applied to parties within a designated RPN, and enforcing that regulation.
- 26 Stakeholders were generally supportive of this approach, including the Commission. They agreed that concentrating the power of designation and regulation with the same entity could risk pre-determining outcomes and prevent the decision-maker from taking a more holistic view of the retail payments system.
- 27 I am also proposing that the legislation allow for amendments to alter the scope of designation or de-designation of RPNs that no longer meet the criteria for designation. The process for amendment and de-designation will be the same as that for making a designation.

The Commission's powers to regulate designated participants

- 28 In April, Cabinet agreed that the Commission would have the ability to impose requirements regarding pricing limits and principles, and agreed in-principle to make directions requiring designated parties to amend their rules or processes (such as rules relating to surcharging or steering by merchants). Following consultation, I consider these powers to be appropriate for the regulator.
- 29 In addition, I propose the following additional powers, so that the Commission has the ability to:
- 29.1. impose information disclosure standards relating to what information should be provided between different classes of participants in a designated RPN;
 - 29.2. impose standards relating to access to parts of the RPN;
 - 29.3. set standards for pricing methodologies;
 - 29.4. where a RPN has no rules, to require the network operator to set rules; and
 - 29.5. issue directions to comply with network rules.

Information disclosure

- 30 Cabinet agreed in principle that the Commission could impose requirements for information to be provided to merchants, consumers or the general public by participants of designated RPNs. I consider that this power should be broadened to also be able to include requirements on what information should be provided by one class of participants to another, to reduce information asymmetries.

Access regimes

- 31 I propose that the Commission should be able to issue determinations to impose access regimes on parts of the RPNs. This would allow the Commission to set open access requirements for aspects of a designated RPN, such as becoming a participant or gaining access to infrastructure. This could be applied to any class of participants in a designated RPN. This would provide the regulator with the ability to require access for new participants in aspects of RPNs, such as for new merchant service providers, or access to switch infrastructure for new entrants to the switch market.
- 32 Currently, due to the comparatively small scale of the New Zealand market, it is difficult for non-banks to offer merchant services or new payment schemes to enter the market and achieve the critical mass necessary to be viable and compete. Additionally, Paymark dominates the switch market, which is the infrastructure that connects the participants of the retail payments system. This forces all payment system providers entering the New Zealand market to negotiate a connection with Paymark.
- 33 Allowing the regulator to intervene to impose access requirements on the operators of a RPN does impact on the property rights of the system operators, in that they have invested in infrastructure which they will be required to provide access to. However on balance, I consider that regulating access regimes would increase

competition and reduce MSF, for example if it results in more competition between acquirers as they compete for merchants' business.

Pricing methodologies

34 As part of its ability to set pricing limits or principles, the Commission should be able to set standards for pricing methodologies, which relate to how prices are expressed. This could be used by the Commission to require certain pricing formats when prices are offered to merchants, which will assist them in comparing offers between providers.

Directions to establish rules

- 35 If a RPN is not governed by any rules I recommend the Commission should be able to require the network operator to establish a set of rules.
- 36 I also consider that substantive rule changes to the network operator's rules should require authorisation by the Commission.
- 37 In conjunction with the power to direct changes to network rules, these powers could be used by the regulator together to improve competition in networks and between networks. For example, should the EFTPOS RPN become designated, these powers could be used to change the RPN to provide for innovation such as contactless and online capability. This would enable EFTPOS to provide competition to the Visa and Mastercard debit RPNs where it currently does not (e.g. contactless and online) and improve the resilience of the EFTPOS RPN. I consider the resilience of a domestic RPN like EFTPOS to be important for New Zealand.

Directions to comply with rules

38 I consider the Commission should have the ability to direct participants in a designated RPN to comply with a network rule. Without this ability, compliance with network rules would be left to private enforcement and the Commission would have no means of ensuring that participants in a designated RPN will comply.

Criteria for exercise of powers in designated RPNs

- 39 In exercising these powers on participants of designated RPNs, I consider that the Commission should have to first consider whether the situation meets specified criteria. For each power, I propose the Commission must have regard to the objectives of the regime in addition to the following specific criteria:
- 39.1. **setting an information disclosure standard** – Being a participant of a designated RPN is sufficient to require application of this standard.
 - 39.2. **setting a pricing standard** – The Commission must consider whether features are present, or likely to be present, in a RPN that are resulting or that are likely to result in the objectives of the regime not being met.
 - 39.3. **setting a standard for access** – The Commission must consider whether features are present, or likely to be present, in a RPN that are resulting or that are likely to result in the objectives of the regime not being met, and consider the effect of intervention on innovation.

- 39.4. **directions to amend and establish network rules** – The Commission must consider whether features are present, or likely to be present, in a RPN that are resulting or that are likely to result in the objectives of the regime not being met
- 39.5. **directions to comply with network rules** – Actual or suspected non-compliance is sufficient cause for the use of this direction.

- 40 In addition to the specific criteria, where a feature needs to be identified (e.g. setting a pricing standard), the Commission should also consider whether the benefits of reducing the deficiency outweigh the costs.
- 41 The Commission will exercise these powers through issuing a legislative instrument, which will set out the purpose and effect of the determination, the participants of the RPN that the determination applies to, and is the requirements on participants.
- 42 The legislation will set out the process the Commission must follow before finalising a determination. The Commission must consult persons who are likely to be affected by the draft determination, by giving them a copy of the draft determination and any supporting documentation, and also making these materials publicly available. Once a determination has been made the Commission must give a copy of the determination to the known parties, make it publicly available, and publish any submissions received on the draft determination (with consideration given to the Official Information Act 1982 and Privacy Act 2020).

Limits on merchant surcharging

- 43 When MBIE undertook targeted consultation with selected stakeholders, a common concern raised was that if merchants continue to surcharge excessively, the benefits of regulation to reduce merchant service fees will not flow through to consumers.
- 44 Under the Fair Trading Act 1986, misleading consumers as to the reasons for a surcharge is prohibited, under the general prohibition against misleading and deceptive conduct. If a merchant represents that a surcharge is for a certain aspect of the cost, the surcharge must relate to that cost. However, stakeholders have emphasised that excessive surcharging for certain credit and debit transactions continues to occur.
- 45 As such, I consider that the Commission should have the ability to regulate the surcharges applied by merchants, in order to limit excessive surcharging that does not reflect the costs to the merchant of providing those particular transaction types.
- 46 I propose this utilise the existing prohibition under the Fair Trading Act, by the Commission issuing standards as to how payment surcharges can comply with the Fair Trading Act, to inform merchants as to what can and cannot be factored into a surcharge. In setting standards which have legal effect, the law will essentially provide merchants that set surcharges in accordance with the standards a safe harbour for compliance with the Fair Trading Act. The Commission would continue to enforce misleading surcharging under the Fair Trading Act.

- 47 Some stakeholders proposed that surcharging should be prohibited altogether, as it may not be justified where interchange fees are regulated. However, regulating the input costs of MSF does not necessarily remove those costs altogether for the merchant. Surcharging, if done reasonably, may still be useful for merchants to steer consumers towards lower cost methods.

Monitoring, enforcement and general powers

Monitoring powers

- 48 I would also like the Commission to have broad powers to monitor and conduct studies into the state of competition in the wider retail payments system. This will be integral to enabling the Commission to effectively monitor the regime and determine when a RPN may need to be designated.
- 49 The Commission would be able to produce public reports on the state of the retail payments system, which could include matters such as levels of merchant service fees in the market. The Commission would also have the ability to require participants in the retail payments system to produce new information to support this monitoring function. These powers align with the Commission's monitoring powers under the Commerce Act.
- 50 Given the purpose of the monitoring and enforcement powers is to enable the Commission to monitor the overall state of the retail payments system, I recommend that the Commission should be allowed to exercise these powers against all participants in the retail payments system (i.e. both those who are participants in designated RPNs and non-designated RPNs).

Enforceable undertakings

- 51 Cabinet has already agreed, in principle, that the Commission should be able to accept enforceable undertakings as an alternative to regulation or to remedy non-compliance. Following targeted consultation, I still consider this power to be warranted, as it provides an alternative pathway to direct intervention. The process for accepting and enforcing undertakings should align with sections 74A – 74C of the Commerce Act (which relate to how the Commission can accept undertakings, which matters undertakings can relate to, and court orders in the event of a breach), while relating to any matter in which the Commission is performing or exercising its functions, powers or duties under the new regime.

Enforcement

- 52 I consider that there should be a range of penalties and remedies available where a breach of the obligations in the regulatory regime has occurred. I propose that pecuniary penalties, injunctions and other court orders including damages and compensation should be made available.
- 53 I propose that injunctions and other court orders should also be made available for a breach of regulatory requirements, including through private action. Injunctions may be necessary to prevent further harm from the contravention of a determination. It may also be appropriate for the court to make other orders in relation to the breach, such as orders to vary a contract.

- 54 The legislation should also make provision for the court to order damages and compensation in the event of a breach. This would be used in the event of contraventions of provisions regarding access regimes and contraventions of some standards, where a remedy is needed for an affected party.

Penalties

55 I propose that pecuniary penalties be available for a contravention of the following requirements. Pecuniary penalties are appropriate for compliance failures that are straightforward. This is consistent with pecuniary penalties for similar compliance failures in the Commerce Act, Fuel Industry Act 2020 and Financial Market Infrastructures Act 2021. The volume of transactions across the New Zealand economy and potential for commercial gain from a breach is significant such that high penalties are appropriate for certain breaches, particularly of price regulation. The legislation will specify maximum amounts where an individual (e.g. a director of a company) is liable, and where a body corporate is liable. I consider these maximum penalties should be:

- 55.1. **Pricing standard:** Where a network operator, payment service provider or infrastructure provider in a designated RPN has failed to comply, they would be liable for maximum pecuniary penalties of \$500,000 for an individual or \$5 million for a body corporate;
- 55.2. **Access standard:** Where a network operator, payment service provider or infrastructure provider in a designated RPN has failed to comply, they would be liable for maximum pecuniary penalties of \$200,000 for an individual or \$2 million for a body corporate;
- 55.3. **Information disclosure:** Where a network operator, payment service provider or infrastructure provider in a designated RPN has failed to comply, they would be liable for maximum pecuniary penalties of \$200,000 for an individual or \$2 million for a body corporate;
- 55.4. **Directions to make or amend rules:** Where a network operator of a RPN has failed to comply, they would be liable for maximum pecuniary penalties of \$200,000 for an individual or \$2 million for a body corporate;
- 55.5. **Directions to comply with network rules:** Where a network operator, payment service provider or infrastructure provider in a designated RPN has failed to comply, they would be liable for maximum pecuniary penalties of \$200,000 for an individual or \$2 million for a body corporate;
- 55.6. **Submission of substantive rule changes to the Commission:** Where a network operator, payment service provider or infrastructure provider in a designated RPN has failed to comply, they would be liable for maximum pecuniary penalties of \$15,000 for an individual or \$150,000 for a body corporate;
- 55.7. **Enforceable undertakings:** Where a body corporate in the retail payments system that is party to an enforceable undertaking (with the exception of the Commerce Commission) has failed to comply with an undertaking, they would be liable for maximum pecuniary penalties of \$500,000;

Enforcement and functional powers brought over from the Commerce Act

56 I propose that the Commission should be able to use the same enforcement and functional powers and provisions as it has under the Commerce Act when carrying out its functions under this Act. This will ensure a common approach to carrying out the functions of the Commission (across the legislation it enforces). I recommend the Bill should confirm the following provisions of the Commerce Act will apply with any necessary or reasonable modifications:

- 56.1. the key investigation powers (e.g. the power to demand information, documents and summons witnesses, the power to search, the power to take evidence, and the power to impose confidentiality orders in sections 53ZD, 98, 98A, 98G, 99 and 100) with the associated protections (e.g. proceedings privileged under section 106)
- 56.2. the general provisions relating to how the Commission operates (e.g. sitting in divisions, ability to state case for court, and service of notices in sections 13, 15-17, 100A, 101, 102 and 109)
- 56.3. the general provisions relating to enforcement (e.g. proceedings for pecuniary penalties and granting injunctions in sections 79A, 88, 88A, 90 and 106A)
- 56.4. the power to disseminate information (section 25)
- 56.5. the provisions relating to the making of determination (section 104)
- 56.6. the provisions relating to assistance to overseas regulators (e.g. 99B-99P), and
- 56.7. that it would be an offence to obstruct the Commission (section 103).

Initial designation of Mastercard and Visa RPNs in the Bill

57 Cabinet agreed to a transitional price path for Mastercard and Visa credit and debit products, to come into force within six months after enactment. To give effect to these decisions, I recommend that the initial designations for the Mastercard and Visa schemes and initial pricing standards be included in schedules to the Bill. This will provide greater transparency for regulated parties as soon as the bill is enacted. Both the initial designations and the initial pricing standards should also be able to be amended, or revoked, through the processes outlined above.

58 I recommend that the designations distinguish between the credit card and debit card RPNs for each scheme. While these payment products operate on the same RPN, the future prospects of each payment product differ slightly (with the use of credit cards slowly declining in New Zealand) and there are different dynamics with each product. As such, taking a more targeted approach to these initial designations will give the regulator greater flexibility and, if desirable, the ability to remove a specific designation in future.

59 I recommend clarifying the scope of Cabinet's decisions to regulate these payment products in the initial designations. In particular, that the initial pricing standard agreed to by Cabinet will only apply to domestically issued cards being used in New

Zealand. I do not have enough evidence to be convinced that fees charged for accepting international cards warrant regulation at this time. Including international cards in the initial pricing standard would also be difficult to enforce given the cards are mostly issued by overseas banks. If merchant service fees continue to be disproportionately high for these card products, the regime would allow the Commission to intervene.

- 60 I also propose that the initial pricing standard in the Bill will not apply to commercial credit cards (i.e. cards issued for business purposes). Banks have advised that commercial cards have additional benefits which impose additional costs on issuers. I consider that the interchange fees currently being charged for commercial credit card products should not be capped without further investigation into the breakdown of these fees, which the Commission will be able to do once the bill comes into force.
- 61 I also consider that the initial pricing standard should not apply to prepaid cards, which includes the likes of Prezzy cards, which are pre-paid Visa cards. The schemes have advised that prepaid cards make up a negligible proportion of transactions and as such, I do not consider they warrant regulation at this time.
- 62 The initial pricing standard should clarify that cards does not just include physical cards but also any payment instrument including tokenised credentials such as virtual cards, including methods like Apple Pay and Google Pay. Targeted consultation highlighted that this was ambiguous and possibly could lead to transactions using a digital wallet from being excluded from the initial pricing standard. I consider this to be consistent with the intention of the Cabinet decision.
- 63 I also recommend that the initial pricing standard clarifies that interchange fee caps applies as a hard cap on each transaction, rather than averaged out across transactions.
- 64 I also recommend that the initial pricing standard clarifies that where contactless debit interchange fees are charged on a cents per transaction basis, rather than as a percentage, the interchange fee should be capped at five cents per transaction. This change will reflect that some large merchants prefer this fee structure and without the change the initial pricing standard would increase their MSF costs.

Inclusion of pricing standards to prevent compensation by schemes

- 65 Alongside the initial pricing standards for Mastercard and Visa products to be included in the Bill, I think the Bill should include an additional aspect to the initial pricing standard to provide that the scheme operators cannot provide net compensation to issuers. By increasing the scheme fees for acquirers and reducing it for issuers a scheme can provide a “net compensation” to the issuer to compensate them for a reduction in interchange income.
- 66 This will address a possible flow-on effect of reducing interchange fees. International experience suggests that schemes are likely to help banks regain lost revenue from interchange fee reductions by increasing scheme fees to acquirers and reducing scheme fees charged to issuers. These fee changes are not currently prohibited by the initial pricing standard that Cabinet has already agreed to for Mastercard and

Visa products. These types of fee changes effectively result in no net cost reductions for banks and other operators providing both issuing and acquiring services.

- 67 Given the likelihood of this risk, I recommend prohibiting net compensation by schemes to issuers in the initial pricing standard. This would prohibit issuers from receiving, directly or indirectly, a net compensation. Compensation should include monetary (i.e. reduced scheme fees) and non-monetary effects (i.e. discounts on rewards, reward programmes offering prizes to customers etc).

Institutional arrangements for coordination with other regulators

- 68 Cabinet invited me to report back on the institutional arrangements for the Commission to coordinate with other regulators of payment systems. The main areas of interface is with the Reserve Bank of New Zealand. This is in relation to its role as regulator of systemically-important payment systems under the Financial Market Infrastructures Act and its new stewardship responsibility to ensure that New Zealanders have access to money and ways to pay that meet their needs in the Reserve Bank of New Zealand Bill (**RBNZ Bill**).
- 69 The Commerce Amendment Bill and RBNZ Bill (both currently in Parliament) include provisions that would allow for information sharing between the two regulators once enacted. This will remove any statutory barriers to coordination. As such, I anticipate that the Commission and RBNZ will enter into Memorandums of Understanding and establish working groups as required to coordinate their statutory functions to the extent that they overlap. I do not consider that any further statutory authority is required to enable coordination.

Institutional arrangements for the Commerce Commission

- 70 I am proposing two additional mechanisms to govern the Commission's role as regulator, in addition to its generic governance arrangements under the Commerce Act and Crown Entities Act 2004.
- 71 Firstly, the Minister of Commerce and Consumer Affairs should have the power to transmit statements of Government policy to the Commission to which it must have regard. This provides the Government with a transparent lever to outline relevant matters of Government policy that are relevant to the Commission's work. A similar instrument is available under the Commerce Act and Telecommunications Act 2001.
- 72 Secondly, I consider that Commission determinations under the Retail Payments System Bill shall be deemed to also be statutorily authorised for the purposes of Part 2 of the Commerce Act. This will ensure that the competition and public interest implications of any regulatory requirements are considered once under the specialist regime.

Financial Implications

- 73 On 12 April 2021 Cabinet agreed to initial tagged contingency funding of \$5 million for the Commission to monitor and enforce the transitional price path (\$4 million in operating funding and \$1 million in capital funding). This comprises \$1 million

operating funding in the 2021-22 financial year, \$3 million operating funding in the 2022-23 financial year, and \$1 million in capital funding.

- 74 The proposals in this paper will have ongoing financial implications beyond 2021-22 to implement the full set of regulatory, educational and stakeholder interventions. The proposals are estimated to cost between \$6 million and \$10 million a year to implement. Confidential advice to Government
- 75 To alleviate some of the costs, I consider that costs incurred to consider and assess enforceable undertakings and review and approve substantive network rule changes should be recovered through fees. The ability to impose fees to recover costs is limited to the exercise of this power given that an enforceable undertaking provides a benefit to an individual participant. To enable this, I am seeking approval for the Bill to include a power to recommend the making of regulations for the Commission to recover, through fees, costs incurred in the exercise of a power at the request of an individual participant. These fees will be set in line with the Treasury's Guidelines for Setting Charges in the Public Sector.

Legislative Implications

- 76 The proposals in this paper will be given effect through the Retail Payments System Bill Confidential advice to Government
In order to meet this timeline I am seeking Cabinet agreement to delegate decisions to me on additional, minor and technical matters, consistent with the general policy intent, that arise during the course of drafting.
- 77 The Act will bind the Crown. I consider the Crown should be excluded from liability for pecuniary penalties. It is unlikely the Crown will participate in the retail payment system as a network operator, payment service provider or infrastructure provider and will therefore not be required to comply with requirements of which contraventions can result in pecuniary penalties. The presumption against imposing criminal fines on the Crown is relevant here, as pecuniary penalties are analogous to criminal fines.
- 78 The initial pricing standard should commence six months after enactment of the Retail Payments System Bill, to allow regulated parties sufficient time to make any necessary changes in order to comply.
- 79 The remainder of the proposals should commence the day after the Royal assent. It is important that the Commission has powers to begin monitoring the retail payments system, to inform any future regulation.

Impact Analysis

Regulatory Impact Statement

- 80 The regulatory impact analysis requirements apply to the proposals in this paper. A regulatory impact statement has been prepared and is attached.

Quality of the impact analysis

- 81 A quality assurance panel with members from the Treasury's Regulatory Impact Analysis Team at the Treasury and the Ministry of Business, Innovation and Employment (MBIE) has reviewed the Regulatory Impact Statement (RIS) "Additional tools for regulating the retail payments system" produced by the MBIE. The panel considers that it **meets** the Quality Assurance criteria.
- 82 The RIS has clearly and concisely described the technical and complex proposals in plain language. Additional tools for regulating the retail payments system have been identified and evaluated against a comprehensive assessment framework. The analysis indicates that effective implementation will depend on the Commerce Commission, as the regulator of the retail payments system, having sufficient resources to support its new functions. While consultation has been constrained due to timing, the risk is mitigated as a range of stakeholders have been consulted via a targeted approach.

Population Implications

- 83 The proposals in this paper will not disproportionately impact distinct population groups (such as Māori, children, seniors, disabled people, women, people who are gender diverse, Pacific peoples, veterans, rural communities, and ethnic communities).

Human Rights

- 84 There are no human rights implications arising from the proposals in this paper. Consistency with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993 will be discussed with the Ministry of Justice during the drafting process.

Consultation

- 85 The Commerce Commission, Treasury, Ministry of Justice, Reserve Bank of New Zealand, Inland Revenue and Financial Markets Authority were consulted on this paper. The Department of Prime Minister and Cabinet (PAG) was informed. MBIE also discussed Australia's experience with similar regulation with the Reserve Bank of Australia.
- 86 The Legislative Design and Advisory Committee was consulted on the design of the regulatory proposals.
- 87 MBIE undertook targeted consultation on the proposals in this paper with 18 key industry participants via individual meetings over a period of two weeks. Stakeholders included the Mastercard and Visa schemes, acquirers and issuers, Retail NZ, Paymark, Buy-Now Pay-Later providers, merchant associations and others. The timeframe for consultation and its form limited the breadth and depth of issues that stakeholders were usefully able to provide comment on. Stakeholders were, for the most part, pragmatic and supportive of the decisions taken by Cabinet so far. Stakeholder engagement largely focused on the proposed approach to designation, the regulator's toolkit and the timeline for implementation of the regime.

88 Prior to the April Cabinet decisions, MBIE received 36 submissions on an issues paper, which reflected the perspectives of a broad range of submitters.

Communications

89 I intend to issue a press release following Cabinet agreement.

Proactive Release

90 This paper will be published on MBIE's web site within 30 business days, subject to withholdings as appropriate under the Official Information Act 1982.

Recommendations

The Minister of Commerce and Consumer Affairs recommends that the Cabinet Economic Development Committee:

- 1 **note** that in April 2021 [DEV-21-MIN-0075], Cabinet agreed:
 - 1.1. to introduce a regime to regulate (on a case by case basis) classes of retail payments system participants, their providers and any associated infrastructure operators;
 - 1.2. that the Commerce Commission be empowered as the regulator for the new regulatory regime;
 - 1.3. that the overall objective of the regime be to ensure the retail payments system delivers long term benefits to merchants and consumers;

Objectives of the regulatory regime

- 2 **agree** that the specific objective of the regime is to ensure that the retail payments system delivers long-term benefits to merchants and consumers through efficient retail payment networks and competition in the supply of retail payment services;
- 3 **agree** that in considering the objective of the regime, decision makers should also, as a secondary consideration, have regard to fair distribution of costs to merchants and consumers and transparency within the retail payments system;

Design of regulatory model

- 4 **note** that in April [DEV-21-MIN-0075], Cabinet agreed that the regime should adopt a designation model to provide flexibility and future-proof regulation;
- 5 **agree** that designation can potentially apply to any retail payment network (excluding cash) in the retail payments system;
- 6 **agree** that a designation captures all the participants in the retail payment network, which includes network operators, payment service providers and infrastructure providers, and captures all payment instruments within the retail payment network;
- 7 **agree** that the Minister of Commerce and Consumer Affairs should be responsible for recommending the designation of retail payment networks to the Governor

General, through an Order in Council, on a recommendation from the Commerce Commission;

- 8 **agree** that the Commerce Commission when making a recommendation to designate a retail payment network designation must consider the following:
 - 8.1. whether designation of the retail payments network is likely to promote the objectives of the regime;
 - 8.2. any features or conduct of the retail payment network that reduces or is likely to reduce competition or efficiency in the supply of retail payment services;
 - 8.3. the nature of the retail payment network being designated which includes consideration of:
 - 8.3.1. the number and value of the transactions that the system presently processes or is likely to process in the future;
 - 8.3.2. the nature of the transactions that the system presently processes or is likely to process in the future;
- 9 **agree** that in making a designation, the Minister must have regard to other regulatory requirements applying to the retail payment network;
- 10 **agree** that the Commerce Commission must consult affected parties and publish the rationale for designation;

The Commerce Commission's toolkit

- 11 **note** that Cabinet agreed that the Commerce Commission would have the ability to impose requirements regarding pricing limits and principles, and agreed in-principle that the Commerce Commission would have the ability to impose requirements regarding information disclosure, accept enforceable undertakings, and make directions to amend rules and systems [DEV-21-MIN-0075];
- 12 **agree** that the Commerce Commission have the power to issue standards imposing the following requirements on participants in designated retail payments networks:
 - 12.1. information disclosure requirements;
 - 12.2. pricing method requirements;
 - 12.3. access requirements;
 - 12.4. pricing limits and pricing principles;
- 13 **agree** that standards can differ in application between retail payment networks, between classes of participants within retail payment networks, and between product types within retail payment networks;
- 14 **agree** that the Commerce Commission have the ability, in regard to a designated retail payment network, to:

- 14.1. direct the network operator to set network rules;
 - 14.2. direct the network operator to seek authorisation before any substantive rule changes are implemented;
 - 14.3. direct the network operator to amend the network rules;
 - 14.4. direct participants of a designated retail payment network to comply with a network rule;
- 15 **agree** that the Commerce Commission must have regard to the objectives of the regime, and the following criteria when issuing standards or directions:
- 15.1. **setting an information disclosure standard** – the party is a participant of a designated retail payment network;
 - 15.2. **setting a pricing standard** – the Commerce Commission must consider whether features are present, or likely to be present, in a retail payment network that are resulting or that are likely to result in the objectives of the regime not being met;
 - 15.3. **setting a standard for access** – the Commerce Commission must consider whether features are present, or likely to be present, in a retail payment network that are resulting or that are likely to result in the objectives of the regime not being met, and consider the effect of intervention on innovation;
 - 15.4. **directions to amend and establish network rules** – the Commerce Commission must consider whether features are present, or likely to be present, in a retail payment network that are resulting or that are likely to result in the objectives of the regime not being met;
 - 15.5. **directions to comply with network rules** – actual or suspected non-compliance of the party;
- 16 **agree** that the Commerce Commission have the ability to issue standards which will apply to merchants detailing what payment surcharging is prohibited for the purposes of the Fair Trading Act 1986 and may differ depending on the retail payment network and the type of merchant;

Monitoring, enforcement, general powers and penalties

- 17 **agree** that the Commerce Commission have powers to monitor and publish reports on the state of the retail payments system;
- 18 **agree** that the Commerce Commission have the power to require participants in the retail payments system to produce new information to support the monitoring function and to provide this to the Commerce Commission;
- 19 **agree** that the Commerce Commission have the power to enter into enforceable undertakings with any participants in the retail payments system, as an alternative to regulation or to remedy non-compliance;

- 20 **agree** that the Commerce Commission will carry out its functions (including enforcement of contraventions) under the regime drawing on its relevant powers and provisions in the Commerce Act 1986 (with any reasonable or necessary modifications), including provisions relating to the making of a determination, and the power to demand information, accept enforceable undertakings, and the offence for obstructing the Commerce Commission;
- 21 **agree** that a contravention of the obligations in the table in Appendix 1 be subject to the corresponding maximum pecuniary penalty amounts in the same table;
- 22 **agree** that the court may make orders in relation to conduct that contravenes or may contravene the regime, including granting injunctions, requiring compliance with the regime, and other orders in relation to contracts, including compensation and damages for affected parties;

Initial designation of Mastercard and Visa retail payment networks

- 23 **note** that in April 2021 [DEV-21-MIN-0075], Cabinet agreed to establish a transitional price path to reduce interchange fees for the Mastercard and Visa credit and debit cards;
- 24 **agree** that the Retail Payments System Bill include initial designations of the Mastercard credit, Visa credit, Mastercard debit and Visa debit retail payment networks, which can be amended, or revoked in the same manner as a designation recommended by the Minister of Commerce and Consumer Affairs;
- 25 **agree** that the transitional price path will be implemented as initial pricing standards which can be amended or revoked in the same manner as a standard issued by the Commerce Commission;
- 26 **agree** that the initial pricing standards include a prohibition on issuers receiving either directly, or indirectly, net monetary or non-monetary compensation from network operators (the schemes);
- 27 **agree** that the initial pricing standards for the designated credit retail payment networks exclude internationally issued cards and commercial credit cards;
- 28 **agree** that the initial pricing standards for the designated debit retail payment networks exclude internationally issued cards and prepaid cards;
- 29 **agree** that the interchange fee caps in the initial pricing standard apply on a per transaction basis;
- 30 **agree** that the reference to 'cards' in the initial pricing standard can include any payment instrument, including virtual cards and tokenised credentials;
- 31 **agree** to include in the initial pricing standard that where a contactless debit card interchange fee is charged by the cents, that interchange fee should be capped at five cents per transaction;

Institutional arrangements for the Commerce Commission

- 32 **agree** that the Minister of Commerce and Consumer Affairs should have the power to transmit statements of Government policy to the Commerce Commission to which it must have regard;
- 33 **agree** that Commerce Commission determinations under the regime shall be deemed to also be statutorily authorised for the purposes of Part 2 of the Commerce Act 1986;

Financial implications

- 34 Confidential advice to Government
- 35 **note** that consideration and acceptance of enforceable undertakings will benefit individual participants, warranting the recovery of costs through fees;
- 36 **agree** to the Retail Payments System Bill including the ability to make regulations allowing the Commerce Commission to recover, through fees, costs incurred to consider and assess enforceable undertakings and review and approve substantive network rule changes;

Commencement

- 37 **agree** that the initial pricing standard come into effect six months after enactment of the Retail Payments System Bill;
- 38 **agree** that the remainder of the proposals come into effect upon enactment of the Retail Payments System Bill;

Legislative implications

- 39 **note** that the proposals will be given effect through the Retail Payments System Bill, Confidential advice to Government
- 40 **agree** that the Retail Payments System Bill provide that the Act will bind the Crown; with the exception of pecuniary penalties, which the Crown shall not be liable for;
- 41 **invite** the Minister of Commerce and Consumer Affairs to issue drafting instructions to the Parliamentary Counsel Office to give effect to the recommendations in this paper;
- 42 **authorise** the Minister of Commerce and Consumer Affairs to make minor or technical changes to the policy decisions in this paper, consistent with the general policy intent, on issues that arise in drafting and passage through the House;
- 43 **authorise** the Minister of Commerce and Consumer Affairs to make additional policy decisions, consistent with the general policy intent, on issues that arise in drafting and passage through the House, Confidential advice to Government

I N C O N F I D E N C E

Authorised for lodgement

Hon Dr David Clark

Minister of Commerce and Consumer Affairs

I N C O N F I D E N C E

APPENDIX 1: PECUNIARY PENALTIES FOR CONTRAVENTION

Obligation	Who is liable?	Pecuniary penalty
Comply with price standard	Participants of a designated retail payment network that are listed either by name or by class of participation in the pricing standard. This may include the network operator, payment service providers and infrastructure providers.	\$500,000 – individual \$5 million – body corporate
Comply with access standard	Participants of a designated retail payment network that are listed either by name or by class of participation in the access standard. This may include the network operator, payment service providers and infrastructure providers.	\$200,000 – individual \$2 million – body corporate
Comply with information disclosure standard	Participants of a designated retail payment network that are listed either by name or by class of participation in the information disclosure standard. This may include the network operator, payment service providers and infrastructure providers.	\$200,000 – individual \$2 million – body corporate
Comply with directions to make/amend rules	Network operator of the designated retail payment network in the direction.	\$200,000 – individual \$2 million – body corporate
Comply with requirement to submit substantive rule changes to Commission for authorisation	Network operator of a designated network in the direction.	\$15,000 – individual \$150,000 – body corporate
Comply with directions to comply with a network rule	Participants of a designated retail payment network that are listed either by name or by class of participation in the direction to comply with a network rule.	\$200,000 – individual \$2 million – body corporate
Comply with enforceable undertakings	Any participant in the retail payments system that is party to an enforceable undertaking (with the exception of the Commerce Commission).	\$500,000 – body corporate