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THIRD ADDENDUM TO ATTACHMENT TO SUBMISSION

The following extracts (26 and 27) are reactions to the 'final decisions' on the reform of bank credit card schemes announced by the Reserve Bank on Tuesday 27 August 2002.

EXTRACT 26

TRANSCRIPT

"PERSPECTIVE" ABC RADIO NATIONAL (29 August 2002)

CREDIT CARD DECISION

Good evening.

I want to talk about credit cards - about Tuesday's decision by the Reserve Bank to regulate credit cards.

If I were asked to give the Reserve Bank a 'tick' or a 'cross' for their recent decision, I would 'tick' the box marked 'very cross'. I am really annoyed with the Reserve Bank and so should you be.

The Reserve Bank -- a known 'protector' of the banks -- has let us down. It gave in to threats from banks and reversed a crucial decision on 'eligible costs' for setting credit-card interchange fees.

The banks would be laughing -- they plea-bargained and they won. The community has no similar scope to threaten the Reserve Bank.

Take no notice of any bank posturing over recent days about a 'tough regulatory regime' forced on them by the Reserve Bank. No such thing has happened. The banks got off light -- unfairly so.

Putting the ACCC back in charge of pricing agreements in the banking industry is the way forward -- no more special deals for banks from a compliant Reserve Bank regulator.

The heart of the matter is the cost of funding the so-called 'free credit' period for credit card purchases. The money at stake is substantial, about $250 million, which is 40 cents for each of the 60 million credit card transactions paid in full each year before the due date. The Reserve Bank should have kept its promise to give that money back to the customers.
Last December, the Reserve Bank said,

> *"… passing the costs of the interest-free period to retailers through interchange*

fees would not meet the Reserve Bank's principles for interchange fee setting"

Now, in August 2002, the Reverse Bank says,

"The Reserve Bank is prepared to include the cost of funding the interest-free period as an "eligible cost" ..... ."

Talk about an about turn. Talk about principles. Talk about gutless. Given a chance to stand their ground and set a much-needed lead for the rest of the world, our Reserve Bank caved in to pressure.

This is bad public policy -- when the world is crying out for better.

What is wrong you might ask?

For something to be a 'cost' there must be a benefit on the other side.

The only customers 'getting' free credit are those who pay their credit card account on time and in full. Free credit is smoke and mirrors nonsense. In the normal course customers pay their credit card accounts on time by drawing against deposits at banks on which effectively no interest is being paid.

In the normal course there is no net cost to banks of funding any interest-free period. Yet the Reserve Bank will allow banks to take a 40cent funding cost for every credit card transaction paid off on time.

There is no appeal against this about-face for which the Reserve Bank offers no persuasive explanation -- and it has no intention of measuring any actual funding costs incurred.

The Reserve Bank now says bank credit card schemes are some 'outsourced store card' -- like a Coles-Myer card. There is no regard for the reality that every retailer must accept bank cards these days -- they are as common as cash. One boggles at how a central banker's mind will bend to allow banks access to fees to which they are not entitled, to recover costs that do not exist.

Much of the media discussion of the Reserve Bank's credit card decision has initially been pointless speculation about retailers 'surcharging' credit card transactions and competition from possible 'new entrants'. Don't believe any of it. It just will not happen in any meaningful way.

The key point about credit card reform is that the Reserve Bank made a move in the right direction but it broke an undertaking to look after the people and chose instead to look after the banks.

It is bad form and bad example.

There may be no right of appeal but I will be asking the Treasurer to review this decision.

Peter Mair 29 August 2002

EXTRACT 27

MEDIA MISREADS CREDIT CARD DECISION

The Reserve Bank sold the community short this week and the mainstream media missed the point.

When announcing its decision on the setting of uniform credit card interchange fees, the Reserve Bank said its criteria was to let banks recover 'eligible costs'. One can then only wonder why the Reserve Bank agreed to include a substantial allowance for the notional but not real 'costs' of 'funding interest free periods'. One might also wonder why the media apparently accepted this without demur.

Can't meet today's deadline, don't bother writing the story.

Journalism is hard work when confronting complex reports like the Reserve Bank's "Final Reforms" of credit card schemes. It is an unnecessarily complex document. Committed to 'full coverage' and 'complete analysis' of such documents on the day, the media is disadvantaged. When news stories 'live' for one-day, the official spin put on complex reports unduly influences the flavour of 'news reports'. Especially so if there has been a prior process of briefing selected 'senior' journalists off-the-record with selected bits of the inside story. 'Twas ever thus -- including for Clark Kent and Dick Tracy.

The media reaction to the Reserve Bank's decision on credit card regulation has been favourable. Up to a point, fair enough. The Reserve Bank did (finally) deliver a decision that will (with considerable further delay) reduce credit card interchange fees by some 40 percent. And, in principle, it will allow retailers to 'surcharge' credit card transactions and otherwise admit 'new entrants' to the business of issuing credit cards.

However, that was not the full story. One story not told was that the Reserve Bank had sold the community short -- that it had given into pressure from banks and abandoned a key 'principle'. One would like to say, "There was a time when the Reserve Bank would 'never' have done that" -- as we now realise, however, "it has always done that".

A point of contention is the reversal of a 'principled' decision to not allow banks to recover, in interchange fees, the 'alleged' costs of funding the interest-free period. That abandonment of 'principles' is worth some $250 million or more to the banks each year -- it is $250 million that should have been returned to the community. The integrity of the Reserve Bank was of course worth even more.

Media reports had the Reserve Bank being induced by 'threats' from card issuers to abandon its principles. I was fearful, the signs were there. Among others naïve, I did not believe it would.
Many would like to know more about the process by which the Reserve Bank came to change its mind on such an important 'principle'.

One could tell from the Reserve Banks' 'media release' on Tuesday that the community was in for a shafting. The proliferation of words of self-praise flashed danger. Remembering that this was about a 'no appeal' price fixing agreement favouring banks, consider the choice of self-assertive words like -- 'objective'; 'transparent'; 'cost based'; 'balanced'; 'normal market mechanisms' and 'the benefit of the community as a whole'. In the circumstances that is abuse of the language. Bring back Winston Smith.

There are issues here. One is about whether a key element of the Reserve Bank decision was wrong. Another is about how the media was 'managed' so that a contentious element in the decision was overlooked. Both these issues are worth running to ground. I regard both as a sad reflection on the state of national affairs in Australia.

Was it wrong?

Was it 'absolutely wrong' for the Reserve Bank to about-face on the principle of allowing banks to include a cost for funding "interest-free periods" in interchange fees for credit card transactions?

Consider the facts.

The practical relevance of the 'interest-free period' is limited to those customers who pay their monthly credit card accounts on time and in full. What is the cost to banks of funding the interest-free period? -- my contention is that this cost is quite low, that in particular it is nothing like 40 cents a transaction and $250 million annually.

A key question is, "Where do they get the money for that?' -- to pay-off the account. Most of the money comes from deposits already with banks. The probabilities are that those 'deposits' are in accounts on which no interest of any consequence is paid. In short, a credit card debt on which no interest is charged, is paid off each month using funds already on deposit on which no interest is paid. This is 'tit for tat' -- there is 'no' cost and no entitlement to revenue to recover 'no' cost.

That's the point. And, last December, the Reserve Bank agreed -- including a funding cost for interest-free credit was said to be against the Reserve Bank's principles. It is against my 'principles' for the Reserve Bank to now let banks 'recover' a cost that does not exist.

Of course there are limited 'examples' and 'instances' of situations where credit card bills are paid on time using funds that were not continually on deposit with the same bank or which were attracting a low rate of interest. The proper focus is the broad scheme of things -- and 'free periods' are normally neither a net cost to banks nor a net benefit to the customers. 'No cost, no price' is a useful adage in price agreements.

I hope I have made the point effectively -- if banks do not incur a material cost when allowing free credit periods, they should not be permitted to take payment of substantial revenue to recover no material cost.

Did the media miss the point?

This answer to this question alone warrants a formal inquiry.

Looking back over recent months it is now clear that the presentation of this issue in the media was 'managed'. The Reserve Bank will not say 'yes' or 'no' to rumour that it engaged PR 'spin doctors' to assist their 'media management' (and so protect the conscience of staff involved).

One AFR 'headline' story in mid-June "Banks cave in on credit card fees" appeared without attribution and seemed to be a misleading beat up by the banks for a dull Monday. It is now better assessed as a well-sourced story, albeit given a 'spin' to divert attention from the truth -- that it was in fact the Reserve Bank that had "caved in" and sold the community short.

How do I know this? Around the same time I circulated and published on 'crikey.com.au', two papers noting a sense of 'unease'. The first explored a distinct sense of unease on the part of the Governor of the Reserve Bank in 'sworn' evidence given to a Parliamentary Committee. The second was about a sensible apprehension of unease in the community if the 'cave in' stories appearing in the media, were in fact well sourced. I had 'read between the lines' and correctly surmised in both of my stories that a plea bargain had been entered -- and all of a sudden the 'media' wanted to talk to me, and me to talk about the 'plea bargain'.

I knew I had got something right but not what. Wrongly, I opined that the banks' plea bargain would be rejected. The journalists on the inside knew it was the opposite but could not tell me -- the Reserve Bank had sold out.

The community was dealt with cleverly, not told the full story immediately but softened up to accept without demur an RBA decision to abandon a 'principle'. Manipulation happens 'in business' and 'in government' -- but we don't like it. The Reserve Bank confronted by banks' intransigence and 'public relations experts' might similarly defend its position. An unfortunate inference in this case is that the Reserve Bank effectively (secretly) decided some months ago to abandon the view that it was against its principles for the funding cost of the interest-free period to be included in the credit card interchange fee.

The community had no reason to feel that the Reserve Bank would abandon its principles. The community was not told forthrightly what was happening and had no way of objecting. Now the community is presented with the fait accompli reality and in a way that brooks 'no appeal'.

There were other diversionary tactics. The Reserve Bank has never come clean on the likely practical irrelevance of either 'surcharging' credit card transactions or easier access for 'new entrants' to the business of issuing credit cards. The Reserve Bank has not even outlined how either of these much-hyped propositions is likely to have any substantial practical relevance. There is a big difference between 'can' and 'will' -- a big difference between bold assertion and credible explanation.

I am disappointed to see the Reserve Bank apparently engaged in behaviour that the community is not normally happy with and which it would not normally associate with the Reserve Bank.

I would like to see the media demanding a proper explanation about banks' "no appeal" rights to keep some $250 million that, last December, was to be given back to the community, the media asking questions about the sense of banks 'recovering' a cost that is not real.

End Piece

There are some principles at stake here -- as there were in various other events that rocked Australia and the world in the past year. Which other 'principles' do we not need any more?

I have not given up hope of having the ACCC put back in charge of regulating banks' pricing agreements. I would encourage others to press the same point.

After all, there are principles involved.

Peter Mair   30 August 2002