



WHITE PAPER SERIES: REGULATORY ENVIRONMENT

Commercial Payments

JULY 2017



About This Series

Through this series of papers, we examine the dynamic and growing commercial payments sector in Australia. This paper expands on the market characteristics covered in the first paper by examining the regulatory environment, including legislation (e.g. interchange), through to regulator-encouraged industry coordination (e.g. the New Payment Platform) and the industry initiatives to self-regulate (e.g. Tokenisation and 3D Secure).

Mastercard has partnered on this series with RFi Consulting (RFi), an independent consulting firm focused on the financial services sector and with a strong specialisation in the payments industry.

Who should read this?



Bankers seeking to increase the depth of commercial banking relationships



Card professionals looking to explore new sector opportunities



Company treasurers who wish to reduce costs, streamline processes and free cash

Overview

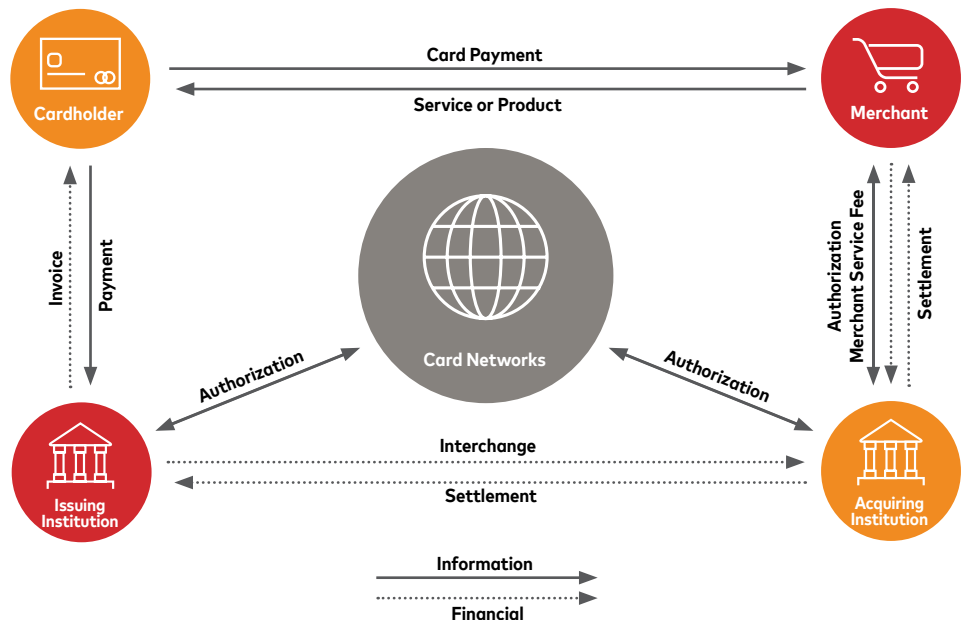
Commercial payments are less regulated than consumer payments, but are still subject to some of the overall regulations which apply to money flows. These include general banking regulations and those that fall under the Anti-Money Laundering and Counter-Terrorism Financing Act 2006 (AML/CTF). All businesses offering designated services (banks and other financial services companies) are required to periodically provide an AML/CTF compliance report to AUSTRAC. The report requires companies to train their staff in risk awareness and due diligence, to have procedures in place for transaction monitoring and risk mitigation, and to ensure the government is alerted to certain transactions – for example, cash transactions of over \$10,000 in value or equivalent in another currency – and transactions from certain countries (currently Iran and North Korea).



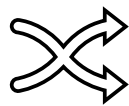
Interchange

Interchange fees are the wholesale fees set by card networks (such as Mastercard and Visa) that require payments between banks (from the merchant's bank to the cardholder's bank) on all transactions – these vary with the type of card, the transaction channel and the type, size and location of the merchant. Some larger merchants are able to gain a more favourable interchange fee level, reducing their cost base and potentially passing this benefit on to their customers. Commercial cards have historically generated higher interchange, which has often been passed back to the company in the form of rebates (usually large corporates) or rewards (usually smaller businesses).

The new regulations **limiting the maximum rate of interchange** on cards to 0.8% may **reduce benefits** passed back to the cardholders, however may also result in a **reduction in the cost of acceptance** of commercial cards for **B2B merchants/ suppliers**.



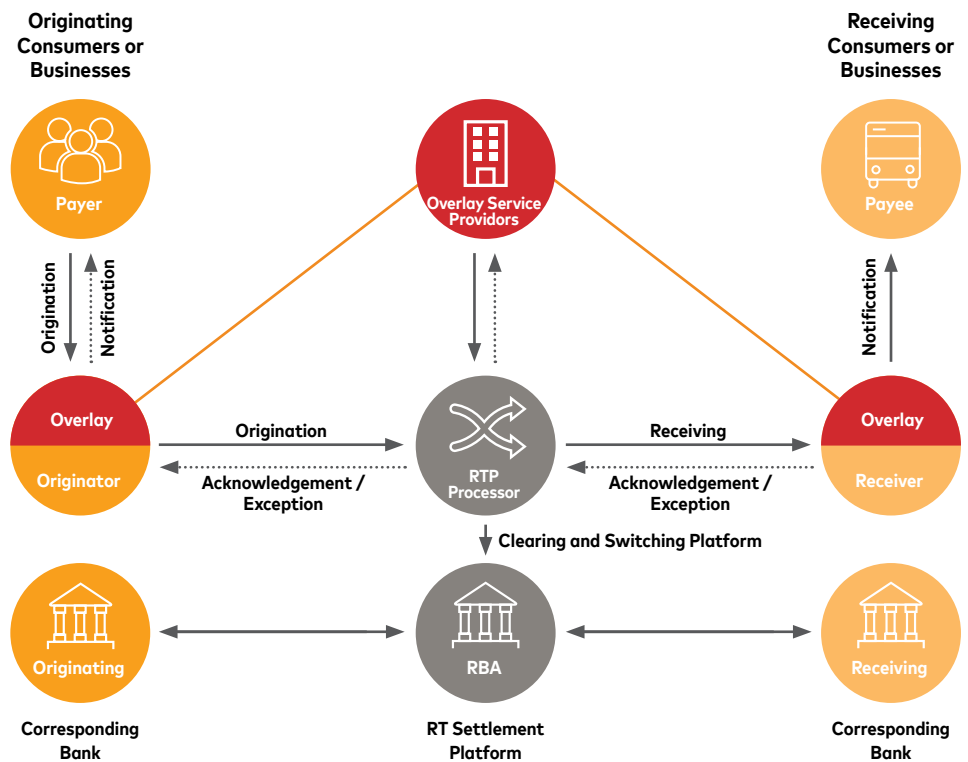
The RBA is currently in the process of modifying these regulations to lower the maximum interchange rates. The new regulations will take effect from 1 July 2017, and will limit the maximum rate of interchange on both commercial and consumer card transactions on Australian issued cards accepted by an Australian merchant to 0.8%. Although this will negatively impact the cardholder proposition on bank-issued cards (and potentially advantage American Express proprietary commercial cards), the change will result in a reduction in the cost of commercial credit card acceptance by merchants. When merchant service fees are lowered, more B2B merchants/ suppliers may be willing to accept cards as a payment option.



New Payments Platform

Due to launch in late 2017, the New Payments Platform (NPP) will be an open access infrastructure for fast payments in Australia. The NPP is being developed via industry collaboration to enable households, businesses and government agencies to make simply addressed payments, with near real-time funds available to the recipient, on a 24/7 basis. Each payment message will be capable of carrying much richer remittance information than existing systems (for instance the 18 characters currently available for Direct Entry payments). The NPP infrastructure will support multiple 'overlay' services that can be independently developed to offer innovative payment services to end-users.

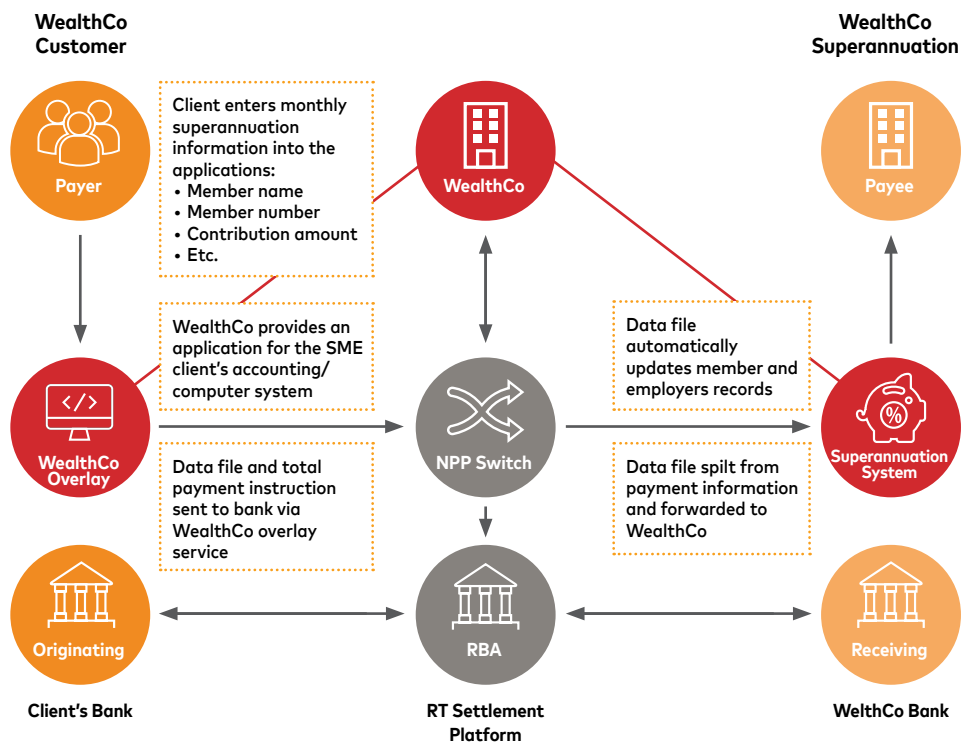
The provision of different **overlay services** is intended to **generate transaction volume**, for example through **mobile payments and e-invoices**, and to provide a variety of **end user interfaces including ERP system integrations**.



Although in itself not generating any new payments in the market, but rather substituting for existing payment methods, the NPP should provide a common foundation on which to base new payment approaches. The proposed data with payment should address needs identified for many years in the B2B market. As a result, more cheques (and cash) may be removed from this sector as electronic payments will be much easier to identify, track and integrate. The NPP “initial convenience service” aims to leverage the mobile channel, and will hopefully deal with the interbank issues of current proprietary bank mobile payment systems.

The addressing of payments without account information (instead using email address, mobile telephone number and/or ABN) should provide ease and convenience and meet the security concerns of some payees. Speed per se may be less of a differentiator, as Direct Entry (EFT) has already moved to 5 times intra-day settlement.

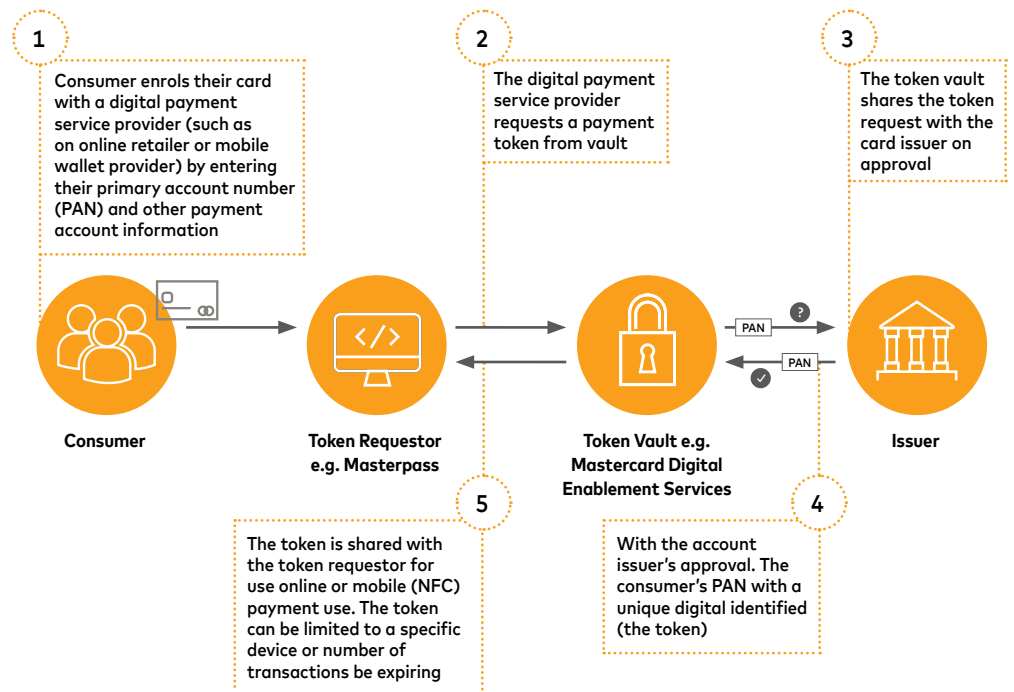
With industry commitment to build the switch, opportunity exists in the overlay service sector. The specifics of the NPP switch and its interface protocols should be published in the near future. However, a number of organisations, for example, BPAY, have already begun developing ideas around overlay services that could be deployed on the new platform. The initial service will be a “credit payment” (push), but debit may follow. As an example, “WealthCo” could have its own overlay service dedicated to its own superannuation clients.





Tokenisation and 3D Secure

Tokenisation as a card security measure has been in use by scheme providers in Australia since 2015. It is a process whereby a random sequence of numbers – a token - in the same format as a real credit or debit card number – is generated for one-time or multiple use. The number used by the merchant and potentially stored in their system is the token number which can only be linked back to the PAN with a decryption key. Hence, the number itself is not at risk.



Generally, the process is administered centrally by the issuing bank and is invisible to the card user and the merchant. However, the merchant can in fact host the server that provides the decryption and token.

3D Secure

The new regulations **limiting** the **maximum rate of interchange** on cards to 0.8% may **reduce benefits** passed back to the cardholders, however may also result in a **reduction in the cost of acceptance** of commercial cards for **B2B merchants/ suppliers**. Furthermore, the implementation of the **NPP** should provide a common foundation on which to base new and innovative payment approaches and the **proposed data with payment** should address needs identified for many years in the B2B market.

3D Secure, known in the market as Mastercard® SecureCode™, Verified by Visa, and American Express SafeKey, is a protocol which offers greater protection for merchants by requiring additional risk-based authentication of a customer's card-not-present transaction. Authentication is via the issuing bank. 3D relates to the three domains involved in the process – the acquirer (merchant's bank), the issuer (card owner's bank) and the scheme provider's infrastructure. To date, Australian enrolment in 3D Secure by merchants has been voluntary but this may soon be mandated, so as to address growing fraud in the online commerce arena.

Next in the series: Virtual Cards Services

For more information contact us at ask@mastercard.com