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Important information

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Proposed New Payments Platform (NPP) Regulations

Submission to the ACCC in support of
NPP Australia Limited's application for
Authorisation

16 February 2017

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1 Executive summary

General The New Payments Platform (**NPP**) is a new domestic platform for the exchange and settlement of simply addressed, data-rich, consumer, business and government payments in near real-time. The development of the NPP facility is a collaborative project between industry and the RBA, which gives effect to the Real Time Payments Committee Proposal that set out a 'path forward' for real-time payments infrastructure in Australia and which was accepted by the RBA's Payments System Board in February 2013.

NPP Australia Limited (**NPPA**) is the industry joint venture company which has funded, built and will operate the NPP. NPPA's member ADIs promote the RBA's and industry's common objectives by building, financing and facilitating open access to the NPP facility by ADIs, non-ADIs and a broad range of consumers, businesses and governments.

The NPP delivers broad public benefits by balancing principles of open access with the requisite balances and checks, (such as eligibility requirements and suspension provisions under its Regulations), to ensure the stability, resiliency, availability, security and integrity of a facility that is required to operate on a 24/7 basis.

Board composition NPPA's governance arrangements have been structured to avoid and manage any potential conflict of interests. Allegations of potential conflict of interests fail to take into account:

- the independence and transparency built into assessments of new participation applications;
- the directors' legal obligation to act in the best interests of the company; and
- the fact that the RBA is represented on the Board (and has been involved throughout the NPP's development); and
- the shareholders' economic incentives to maximise return (which is aligned with NPPA's strong financial incentive to secure high volumes of transactions).

Governance arrangements for the company (and the relationship between the Board and management) are also clear and consistent with best practice.

Eligibility and licensing requirements The 'sound and secure' eligibility requirement is critical to facilitating fair and open access to the NPP facility, while at the same time minimising any possible risks to the stability, resiliency, availability, security and integrity of the system. It is consistent with international standards, a well-understood (and commonly used) concept, and a reasonable risk-based requirement.

Further, there are strong safeguards in place to ensure that NPPA's eligibility criteria will not be applied in a manner that disadvantages prospective NPPA members. RBA oversight as the payments system

regulator and through its Board membership and ongoing observer status also serves to strengthen the existing balances and checks in place.

The 'ADI requirement' is necessary to ensure that relevant participants have the technical, operational and legal capability to perform the NPP's Core Functions (as set out in the Real-Time Payments Committee proposal accepted by the RBA's Payment Systems Board in February 2013) – which is the purpose for which the basic infrastructure has been created.

In any case, the NPP has been designed to enable participation by non-ADIs (as Connected Institutions and Overlay Service Providers) in a way that promotes flexibility, competition and innovation in the public interest. The ADI requirement is therefore not excessive and in fact facilitates the provision of services by non-banks and other service providers.

Suspension and termination

The proposed suspension and termination provisions are reasonable and indeed necessary to maintain the viability of the NPP system. They are also a 'last resort' mechanism, which the Board will not apply except on the occurrence of significant default. Similar provisions exist in all payment systems (and are consistent with best international practice), including those administered by the Australian Payments Clearing Association Limited (**APCA**) (and approved by the ACCC).

NPPA submits that the phrases 'adversely affect' and 'contrary to the interest of' are drafted with sufficient specificity to limit the scope of the Board powers while at the same time retaining a degree of flexibility that would be necessary if an event requiring suspension or termination took place.

Participants' relationships with third parties

NPPA has been designed to have appropriate governance arrangements that ensure the company is able to operate and meet its objectives efficiently and effectively. Its arrangements allow for adequate levels of visibility and transparency to industry and third party stakeholders, as well as flexibility so broader industry consultation can be implemented as needed. The RBA representation and ongoing observer status on the Board also allows representation of broader policy objectives (and thus broader stakeholders) into the decision-making processes of the Board, as does the presence of independent Directors.

To the extent that the arrangements established by the NPP Regulations fail to deliver expected public policy outcomes, the RBA may be expected to exercise its regulatory powers under the *Reserve Bank Act 1959* and the *Payment Systems (Regulation) Act 1998*.

Costs incurred by Participants

NPPA is funded privately and needs to be financially viable to operate. As such, fees and charges need to be levied to cover the company's costs of building the infrastructure as well as ongoing operation costs. However, the company offers a variety of fee structures and options. At the same time, participants in the NPP must have a degree of financial viability to be able to operate. The fee structure therefore provides an adequate balance in terms of securing the financial viability of the business while at the same time ensuring that fees and charges are not excessive and do not create unnecessary (or anti-competitive) barriers to entry. NPPA's publicly

available strategic blueprint positions the infrastructure as economically self-sustaining (not profit-maximising).

2 Board composition

2.1 Market feedback

We understand the ACCC has received feedback expressing concern that the composition of the Board of NPPA may result in a conflict of interest between the goals of the NPP (i.e. increasing participation for the benefit of consumers) and Board members (who are responsible for decisions about the suspension or termination of a person's right to be an NPP Participant, Connected Institution or Overlay Service Provider) furthering the interests of their employers by restricting access by new entrants to the NPP.

We further understand that those submissions have expressed a view that the Board composition should reflect a broader scope of industry representation across incumbents, regulatory agencies, executive management, new entrants and government agencies responsible for fostering innovation and development.

Finally, it has been noted that the NPP Regulations do not expressly state how the Board's decision making powers will be devolved to management, and accordingly it is difficult to assess potential risks regarding the impartiality of decision making.

2.2 Background

(a) Introduction

As noted in the applications for authorisation lodged in October 2016 (the **Application**), the New Payments Platform (**NPP**) is a new domestic platform for the exchange and settlement of simply addressed, data-rich, consumer, business and government payments in near real-time. The architecture, features and functionality of the NPP were initially developed in response to the RBA's strategic objectives on payments innovation and in accordance with the principles set out in the Real Time Payments Committee (**RTPC**)'s 2013 Proposal on innovation in the payments system.¹ Importantly, the layered architecture of the NPP is designed to promote competition and drive innovation in payment services, and also respond to the evolving needs of Australians in the digital economy, now and in the future.

Since 2013, the industry, together with the RBA, has worked collaboratively towards the realisation of the RTPC Proposal, in terms of:

- building new technology and infrastructure to enable real-time orchestrated messaging between the RBA's purpose-built settlement facility (the **FSS**) and Australian Authorised Deposit-taking Institutions (**ADIs**);
- ensuring the immediate availability of a payment service using the NPP that ADIs connected to the NPP and payment service subscribers can offer consumers, businesses and governments via the payment service provider BPAY (the **initial convenience service** or **ICS**); and

¹ <http://www.apca.com.au/docs/real-time-payments/real-time-payments-proposal.pdf>

- building governance frameworks to more generally enable the development of overlay services and access for non-ADI approved entities to access the NPP to deliver innovative payment services and realise the NPP's benefits.

(b) NPP Design Features

The technology, equipment and infrastructure assets needed to operate the NPP have been developed and built, and will be operated, by SWIFT under the terms of a 12-year services contract.² The assets are owned by an industry joint venture company, NPP Australia Limited (**NPPA**) (discussed further below), which is responsible for operating and managing them in accordance with its constitutional objectives.

The platform will support the interbank exchange of orchestrated ISO 20022³ financial messages to effect the near real-time clearing and settlement of:

- credit transfers between connected NPP Participants⁴ in accordance with minimal SLAs/requirements (**Basic Single Credit Transfers** or **BSCTs**); and
- credit transfers between connected NPP Participants (either for themselves/own customers or for the third party institutions to which they provide NPP clearing and settlement services) associated with 'overlay payment services' (**Overlay Service Payments**). Overlay services are proprietary payment services, which could be commercial or compliance-focused services, which are owned and operated by third parties on proprietary terms, but consistent with the common standards and requirements set out in the NPP Regulations and NPP Procedures.

The ISO 20022 message set also includes a range of 'non-value' messages, such as those relating to payment initiation, inquiries and investigations. These 'non-value messages' can be used in relation to BSCTs and overlay payment services.

The RBA is a founding member of the company and has been involved in the program since its inception, and has recognised, and acknowledged, how complex, far reaching and costly the project is, both in terms of the central infrastructure build and the integration effort required to be made by participating ADIs.⁵ The RBA is also the provider of the Fast Settlement Service (**FSS**), new functionality within the Reserve Bank Information Transfer System (**RITS**) that enables gross settlement of NPP Payments immediately following clearing.

The platform includes a separate, highly secure addressing service which is owned and operated by NPPA. The addressing service meets the objectives of the RTPC proposal in relation to simple addressing of payments. The service will support the secure and access-controlled registration of customer account information and proxies which resolve to account information (such as telephone numbers, email addresses and company numbers), enabling BSCT initiation and Overlay Service Payment initiation by consumer, business and government payers by use of a proxy, as well as by BSB/account numbers if the payer prefers to do so.

² SWIFT is a member-owned cooperative that provides the communications platform, products and services to connect more than 10,500 banks, securities institutions and corporate customers

³ ISO 20022 is a financial services messaging standard that was developed within the International Organization for Standardization (ISO). The standard is intended to become the first globally interoperable messaging standard. (<http://www.apca.com.au/docs/policy-debate/iso-20022-implementation-best-practices.pdf>)

⁴ For the purposes of this submission, 'NPP Participant' is a reference to a member or shareholder of NPPA.

⁵ <http://www.rba.gov.au/speeches/2014/sp-gov-231014.html>

(c) Initial Convenience Service

The rationale for the NPP architecture and the importance of an ICS is well-documented in publicly available materials.⁶

The RTPC Proposal provided that:

“the initial convenience service will be developed by end 2016 as one of the first overlay services. The intent is to ensure that a compelling proposition for use of the basic infrastructure is available as soon as possible. The design of this service will depend on its commercial evolution, whether it is provided by an existing payment service or scheme, or developed from scratch. However, the Committee’s intention is that it will focus on personal convenience payments, particularly those using mobile channels. This service will need to offer enough business and operational support for ADIs to deliver an attractive value proposition to their customers. It will need to consider the merits of:

- *specific rules relating to end customer service expectations, such as the obligation to post to an account and inform the payee in a very short timeframe;*
- *inter-ADI commercial arrangements such as incentive or interchange payments;*
- *technology to support payment products and channels attractive to particular user groups;*
- *branding, business development and marketing programmes; and*
- *inter-ADI risk management, fraud prevention and dispute resolution as appropriate for the particular services provided. The initial convenience service will be open to all ADIs to join as they see fit. However, ADIs will always have the option to initiate and receive real-time payments directly through the basic infrastructure.”*

NPPA conducted a competitive tender process and selected BPAY to develop and deliver the initial convenience service to launch at around the same time the platform is delivered by SWIFT.

[REDACTED]

All ADIs and financial institutions that ‘indirectly’ connect to the NPP through a connected NPP Participant will be able to subscribe to the ICS and make the services available to their customers also.

The coordinated delivery of the two parts of the NPP programme – platform and an immediately available payment service – is designed to enable all ADIs to be able to offer a viable service to consumers, businesses and governments from its launch in October 2017.

(d) Overlay Services and Connected Institutions

The ICS is not expected to be the only payment service operating on the platform, and ADIs are not expected to be the only connected users. The NPP Regulations establish an open access framework for any eligible body corporate that wishes to participate in the NPP, without having to become a shareholder in NPPA, either:

⁶ RTPC proposal , PSB response etc

- to offer overlay services (as an ‘**Overlay Services Provider**’); or
- to connect to the platform for the purposes of utilising the its non-value messaging functions (as a ‘**Connected Institution**’).

The access arrangements for Overlay Service Providers are designed to enable any company which has a payments service proposal and which meets the eligibility criteria to be admitted and its services recognised in the NPP Business Reference Data Tables.

NPPA management has delegated administrative responsibility, from the Board, for the assessment and determination of any participation application submitted by a prospective Overlay Service Provider who intends to use the NPP basic infrastructure ‘as is’ (in the NPP Regulations, these are described as Level 1 Overlay Services)⁷. The access arrangements for Overlay Service Providers are also designed to accommodate and encourage innovation by any prospective Overlay Service Provider whose proposal requires some level of agreed modification to the NPP itself (such as a new message type, or a reorchestration of the standard NPP message flows)⁸.

Each overlay service is differentiated and identified in the NPP by a unique identifier and by its own closed user group of NPP Participants that either subscribe to or provide clearing and settlement services for that overlay service. However, for the purposes of admission, an applicant does not need to have committed subscribers (NPP Participants or third parties).

Overlay services are not expected to be confined to commercial services. The overlay service model has a range of applications in regulatory and compliance activities, and may deliver significant efficiencies and enhance regulatory outcomes across a number of key portfolios. AUSTRAC has provided NPPA with the following statement⁹ outlining its understanding of how the NPP may enhance regulatory activity:

“AUSTRAC understands the transformative nature of the New Payments Platform (NPP). As Australia’s financial intelligence unit and AML/CTF regulator, the collection, analysis and dissemination of actionable financial intelligence to AUSTRAC’s law enforcement partners is essential in combatting and disrupting serious and organised financial crime and terrorism financing. Our mandate is to detect, understand and disrupt in this space and as such, AUSTRAC is keen to explore the potential opportunities that may arise from the NPP, in particular any additional information captured by virtue of the system which is being built in compliance with new international messaging standards. Of equal importance, is the need to understand the risks that may arise from the NPP implementation and work proactively and collaboratively on mitigation measures.

AUSTRAC is committed to a collaborative relationship which will foster trust, build a shared understanding of money laundering, terrorism financing and associated criminal risks; to explore innovative approaches to detecting and mitigating those risks; and to explore options for smarter regulatory outcomes to reduce the compliance burden on the regulated businesses.”

An Overlay Service Provider may also connect to the platform (provided it meets the criteria to be a Connected Institution) for the purposes of streamlining payment processing by injecting its own non-value messages into the infrastructure.

⁷ The delegation becomes effective in practice upon commencement of the NPP Regulations.

⁸ Draft Regulation 4.9, 4.10 and 4.11

⁹ AUSTRAC has provided consent to the inclusion of this statement in this submission.

The access arrangements for corporates that wish to connect to the NPP as Connected Institutions are similarly deliberately minimal. Any company which meets the eligibility criteria may connect to the NPP (using NPP componentry supplied by NPPA and SWIFT), not for the purposes of injecting clearing and settlement request messages into the NPP, but for the purposes of utilising the NPP's non-value messaging functionality (such as the ability to send and to receive payment initiation requests for account-holder authorisation, ICS payment requests, inquiries and so on). The potential efficiencies and benefits to corporates of partnering with an NPP Participant for clearing/settlement and connecting to the platform to offer payment initiation services and leverage enhanced data capabilities for straight through processing are manifold.

(e) NPPA

As noted above, NPPA is the company with the responsibility for the operation of the NPP. NPPA's objectives (as noted in its Constitution) include establishing and operating the NPP in a manner that promotes the public interest by:

- ensuring the safe, reliable and efficient operation of the NPP;
- facilitating fair access to the NPP as a mutually owned utility infrastructure; and
- ensuring ongoing investment in the NPP to meet the changing needs of financial institutions and users of Australian payments systems.

The operations of the NPP are governed by the NPP Regulations and NPP Procedures, which operate as a multi-lateral contract – a set of obligations between each participant and NPPA, and between participants.

While NPPA owns and operates the NPP infrastructure, it will not itself own, operate or provide overlay services to be offered using the NPP.¹⁰

(f) Governance arrangements

(i) Introduction

Governance arrangements for NPPA and the NPP include:

- a Constitution and Shareholders Agreement that set out the governance framework for NPPA (e.g. process for passing Board decisions, appointing directors);
- the NPP Regulations that govern the rules of access and participation in the NPP, including high level obligations in relation to basic infrastructure, clearing transactions and settlement;
- the NPP Procedures (that cover operational or technical practices, procedures, standards and specifications, detailing how obligations in the NPP Regulations are to be met); and
- a management committee structure that will enable NPPA to continue to utilise industry resources (NPP Participants' technical experts who have been made available throughout the NPP programme) once the NPP is operational.

¹⁰ Note that NPPA will ensure the NPP supports the basic interbank service which is contemplated as part of the NPP infrastructure. However, commercial and compliance services will generally be provided in the form of 'over-the-top' or overlay services.

(ii) Participation in NPPA

Members

Under the NPP Regulations, NPP Participants are required to be or to become shareholders in the company, and to subscribe for redeemable preference shares in NPPA to fund the costs of building and initial operation of the NPP. As noted in the Application, NPPA currently has 13 shareholders, or 'members'.

Membership is categorised according to level of overall payments system participation and investment in the NPP infrastructure:

- **'High' participants: [REDACTED]** There are currently four 'high' band members in total, comprising Australia and New Zealand Banking Group Limited, Commonwealth Bank of Australia, National Australia Bank Limited and Westpac Banking Corporation;
- **'Medium' participants: [REDACTED]** There are currently seven 'medium' band members in total, comprising Reserve Bank of Australia, Cuscal Limited, Bendigo and Adelaide Bank Limited, Citigroup Pty Limited, ING Bank (Australia) Limited, Macquarie Bank Limited and HSBC Bank Australia Limited;
- **'Low' participants: [REDACTED]** There are currently two 'low' band members in total, comprising Australian Settlements Limited and Indue Limited,

At General Meetings, ordinary members' resolution are passed by approval by members (irrespective of the class of shares held) present and voting who between them hold more than 66% of the total number of Shares (excluding disqualified members); while special majority members' resolution require 75%.

Non-members

As detailed at section 2.2(d) above, consistent with principles of fair and open access, non-member parties can also have a degree of participation in the operations of the NPP without having to subscribe for shares in the company, as follows:

- as a Connected Institution ie. a body corporate connected to the NPP 'basic infrastructure' solely for the purposes of sending and receiving non-value messages; and
- as an Overlay Service Provider ie, a body corporate that will provide an overlay service.

(iii) Board representation for NPPA members

The NPPA Board was formed in December 2014, with an Independent Chairman, Paul Lahiff, appointed in November 2014,¹¹ and Adrian Lovney, appointed as the CEO of NPPA in September 2016¹², replacing the APCA appointee.

Members are responsible for appointing directors to the Board. Schedule 2 of NPPA's Constitution prescribes that matters including the appointment or removal of directors require a 75% majority member vote.

¹¹ <http://www.nppa.com.au/about-npp-australia/npp-australia-board/>

¹² <http://www.apca.com.au/docs/default-source/2016-media-releases/npp-media-release---npp-australia-appoints-inaugural-ceo>

The rights conferred upon each member to appoint a director to the Board are determined by the extent of their investment in the NPP (with the exception of the RBA). Accordingly, there is currently a total of 11 directors (including the independent Chairman and CEO) who have been appointed as follows:

- each of the 'high' band members has the right to appoint a director (four directors appointed, one from each of ANZ, CBA, NAB and Westpac);
- 'medium' and 'low' band members collectively have the right to appoint four directors between them by an election process, with 'medium' band members allocated twice the number of votes as 'low' band members (four directors appointed, one from each of Cuscal Limited, Bendigo & Adelaide Bank Limited, ING and Citigroup Pty Limited); and
- the RBA currently has the right to appoint a director and, from the time the NPP becomes operational, an observer, to ensure adequate regulatory oversight and involvement in the NPP's governance. Currently, the RBA Head of Payment Settlements is appointed as director and the RBA Head of Payments Policy is appointed as the alternate director. The NPPA Board has in recent months been actively considering a proposal, subject to shareholder approval of requisite constitutional amendments, to extend the RBA's right to appoint a director beyond the date the NPP becomes operational by giving it the right to appoint the Head of Payment Settlements as a director in recognition of the importance of the FSS to the NPP.

In addition, *one additional independent director* is to be appointed in accordance with the Shareholders Agreement, with effect from the date the NPP becomes operational¹³.

New members will be classified as either 'medium' or 'low' participants and will be eligible to participate in the election of directors.

[REDACTED]

(iv) Operations of the Board

As noted above, directors are appointed by members and represent members. Article 10.9 of the Constitution specifically recognises that directors may consider the interests of any Member or group of Members who appointed, elected or selected them in making any decisions. Nevertheless, this is still subject to any obligations at law, including those under the Corporations Act 2001 (Cth) (**Corporations Act**). Specifically the Corporations Act and common law provides that each director has duties:

- to act for a proper purpose and in the best interests of the company (section 181); and
- not to improperly use their position as a director to gain an advantage for themselves or someone else or to cause detriment to the company (section 182).

Pursuant to article 10.8 of the Constitution, at directors' meetings each director (including the Independent Chairperson and the second independent director) has one vote, other than the Executive Director (as defined in the Shareholders' Agreement) who is not entitled to vote. Decisions are passed by a 66% majority.

¹³ Approximately October 2017

As it is the case with most corporations, under the Constitution the Board has the power to delegate the day to day management of the company.¹⁴ In the case of NPPA, it is intended that day-to-day management and operations of the company and the NPP will be devolved to management supported by an Operating Committee.¹⁵ In the case of assessment and determination of Level 1 Overlay Service Provider applications, the Board has delegated its functions and powers under the proposed NPP Regulations to management. In addition, the management of certain operational issues is delegated to management and the NPP Incident Response Group, comprised of suitably qualified representatives of NPPA, NPP Participants, SWIFT and RBA and is established to manage and resolve technical and operational incidents (i.e. an outage, data or security breach or inaccessibility to facilities via which NPP payments or non-value messages are sent or received).¹⁶

2.3 Response to feedback

Taking the context and background information provided above into account, NPPA provides the following responses to market feedback:

(a) *NPPA's governance arrangements have been structured to avoid and manage any conflict of interests*

Allegations that there may be a conflict of interest between the objectives of NPPA and the members of the Board are ill informed. In particular, they fail to take into account that:

- in order to operate successfully and to ensure that the shareholders maximise their return on their investment, the company has a strong financial incentive to secure high volumes of transactions. This means that the economic incentives of shareholders (ie, maximise return on investment) and the objectives of the company (ie, efficient operation of the company, fair access, etc) are aligned. In this context, the behaviour alleged by market feedback (ie, inappropriate decisions as to membership, suspension and termination) would effectively be contrary to the financial and economic interests of the company and its shareholders;
- the composition of the Board helps minimise any questions or risks of conflict of interest (see further details below). In this context, the behaviour alleged by market feedback would also assume that representatives of the RBA and the independent directors would be ineffective in performing their role;
- there is a mechanism in place to assess new applications that will ensure the process is clear and transparent, and has built-in safeguard mechanisms (see 3.2(c) below); and
- directors are required by law to act in the best interests of the company. Failure to do so could have serious repercussions for the individuals involved. Allegations that the directors would act in breach of their legal obligations are simply baseless.

(b) *The composition of the Board already ensures appropriate representation*

¹⁴ Under Article 9.6, Directors may delegate any of their powers, other than powers required by law to be dealt with by Directors as a board, to a Committee.

¹⁵ Under NPP Regulation 1.1, 'NPP Management Committee' is defined as 'the standing sub-committee of the Board established according to its terms of reference to undertake day-to-day management and operations of the NPP Basic Infrastructure.' It is currently proposed to re-name this the 'operating committee' and have it operate under CEO delegated authority rather than as a Board sub-committee.

¹⁶ NPP Regulation 1.1.

As noted above, decisions as to the composition of the Board have been made to take into account the need to ensure that NPPA:

- is operated efficiently and effectively (including ensuring the company meets the objectives for which it was created and for which shareholders invested in it);
- has sound governance arrangements; and
- meets the broader policy objectives for which it was created.

In this context, the Board provides appropriate representation for:

- all shareholders, especially minority ones, at a level that is appropriate for, and commensurate with, their investment;
- the relevant regulator (ie, the RBA); and
- the broader payment industry (ie, CEO and independent Chair, second independent director to be appointed in October 2017).

(c) *Governance arrangements for the company (and the relationship between the Board and management) are clear and well understood*

As provided for in the Constitution, the Board has the power to delegate day-to-day management activities of the company.

In this case, such delegation will be effected in a manner that is consistent with industry practice (and using the model applied by APCA, which is well understood in the industry and has proved useful and appropriate for many years). In particular, day to day management of the NPP will be delegated to management and its operating committee, as outlined at section 2.2(e)(iv) above.

3 Eligibility and licensing requirements

3.1 Market feedback

We understand the Commission has received market feedback suggesting that the eligibility requirement at 4.2(g)¹⁷ contains an undefined term 'sound and secure' that could potentially be applied in a manner that disadvantages prospective NPPA members; and that the assessment of whether a potential participant's operations are 'sound and secure' should be undertaken by independent experts.

The same feedback has also questioned the rationale for the requirement that NPP Participants be ADIs and argues that the NPP infrastructure should be open further to allow secure, registered and tested entities who are not ADIs to effect payments on behalf of account holders. The feedback has also suggested that the NPP should be open to non-bank payment providers to enable consumers to take advantage of non-bank technologies using the NPP network in competition with card issuing businesses.

¹⁷ Whereby all NPP Participants must, amongst other things, demonstrate, to the reasonable satisfaction of NPPA that its business practices and operations will be sound and secure and will not adversely affect the integrity, security, efficiency, reliability or stability of the NPP Basic Infrastructure.

3.2 Background

(a) Types of participants

Prospective members can participate in the NPP in a number of capacities:

- participants which are connected directly to the NPP for the purpose of sending and receiving NPP payments and non-value Messages, but have not been authorised by the RBA to use the FSS for settlement of NPP Payments (and therefore use the services of another NPP Participant to settle their NPP Payments) (**Clearing Participants**);
- participants which are not connected to the NPP but are authorised by the RBA to use the FSS for settlement of NPP payments (**Settlement Participants**); and
- participants which are connected to the NPP and authorised by the RBA to use the FSS for settlement of NPP Payments (**Full Participants**).

Additionally, a prospective non-member may participate as a Connected Institution or Overlay Service Provider, as outlined at section 2.2(d) above.

(b) Eligibility criteria

Prospective members participate as NPP Participants subject to the following eligibility requirements (under Regulation 4.2):

- be the RBA or an Australian Authorised Deposit-taking Institution [considered further at section 3.3(b)below] [Regulation 4.2(a)] (**the ADI Requirement**);
- be or become a Member and execute an agreement by which they accede to the Shareholders' Agreement [Regulation 4.2(b)];
- be able to comply with any applicable laws, the Constitution, the Shareholders Agreement, the NPP Regulations and the NPP Procedures [Regulation 4.2(c)];
- agree to pay all fees, costs, charges and expenses which may be levied on participants in accordance with the NPP Regulations [Regulation 4.2(d)];
- agree that on becoming an NPP Participant, the NPP Regulations and NPP Procedures will constitute a contract between them and NPPA, and between them and other NPP Participants and Overlay Services Providers [Regulation 4.2(e)];
- agree to act in good faith in the exercise of its rights and performance of its obligations under these Regulations and the NPP Procedures [Regulation 4.2(f)];
- demonstrate that its business practices and operations will be sound and secure and not adversely affect the integrity, security, efficiency, reliability or stability of the NPP 'basic infrastructure' [Regulation 4.2(g)]; and (**the 'sound and secure' eligibility requirement**); and
- be solvent and otherwise able to meet the financial and other obligations imposed on NPP Participants by the NPP Regulations and the NPP Procedures [Regulation 4.2(h)].

Full Participants and Clearing Participants are subject to the following additional requirements (i.e. excluding Settlement Participants) [under Regulations 4.3(a), (c), 4.4(a), 4.6(h)]:

- to become a SWIFT member;
- to enter into a network connection and services agreement with at least two network connectivity service providers; and
- to obtain authorisation by the RBA to use the FSS (which is owned and operated by the RBA) for settlement and having access to an Exchange Settlement Account (**ESA**) for settlement.

As noted above, prospective non-members may also participate as Connected Institutions and Overlay Service Providers, which are subject to eligibility requirements under Regulations 4.6 and 4.8 (largely mirroring those under Regulation 4.2, as outlined above). **However, importantly, these participants are exempt from the ADI Requirement and the requirement to become a shareholder member of NPPA (under Regulations 4.6(a) and 4.8(a), any 'body corporate which carries on business at or through a permanent establishment in Australia' may participate as a Connected Institution or Overlay Service Provider).**

(c) Process for applying for membership

NPP Participants and Connected Institutions apply for membership according to the following steps [under Regulation 4.7(b)]:

- **Step 1:** Send a valid and completed participation application to the NPPA Secretary, providing sufficient information to demonstrate that the applicant has satisfied the applicable eligibility requirements and paying an application fee to NPPA at the time of submission.
- **Step 2:** The Board considers all participation applications and shall accept, on a preliminary basis, each applicant which it reasonably determines satisfies the eligibility requirements.
- **Step 3:** Within five business days of receipt of the participation application, the NPPA Secretary will notify the applicant in writing:
 - of the Board's determination under Regulation 4.7(c); and
 - if the Board determines that an applicant does not satisfy the eligibility requirements, of the reasons for its determination and the review procedure available.
- **Step 4:** In the event of an adverse Board determination, an applicant may:
 - within 3 months, request that a sub-committee of the Board review the participation application (or relevant part) and its determination; or
 - at any time, lodge a fresh participation application.

Overlay Service Providers apply for membership according to the following steps (under Regulation 4.9):

- **Step 1:** Provide to NPPA:
 - sufficient information to demonstrate that the applicant satisfies the eligibility requirements;

- a technical specification for the proposed overlay service (including details of any change to the NPP facility which the applicant considers necessary to support the overlay service);
 - a draft Project Plan for testing and implementing any such change to the NPP facility if the application is approved;
 - a copy of the draft rules for the overlay service; and
 - pay an application fee to NPPA at the time of submission.
- **Step 2:** The Board (or Management, in the case of a 'Level 1' Overlay Service) considers applications within 5 days of receipt and shall accept an application which it reasonably determines satisfies the eligibility criteria.
 - **Step 3:** In the event of an adverse determination, the Board (or Management as applicable) must provide reasons for the decision and an applicant may:
 - within 3 months, request that a sub-committee of the Board review the participation application (or relevant part) and its determination; or
 - at any time, lodge a fresh participation application.

It is intended that the Board will assess new applications from prospective NPP Participants and Level 2 or Level 3 Overlay Service Providers (being more complex, requiring more system development and having more associated systemic risk). However, the Board's discretion to assess applications from new applicants will ultimately be limited by the safeguards which require that, in the event the Board makes an adverse determination:

- reasons must be provided for its determination (Regulation 4.7(d)(ii) and Regulation 4.9(d)); and
- an applicant is entitled to request that a sub-committee of the Board review their application and its determination, or lodge a fresh application (Regulation 4.7(d)(i) and Regulation 4.9(d)).

3.3 Response to feedback

(a) Requirement that NPP Participants be "sound and secure"

NPPA submits that the 'sound and secure' eligibility requirement under Regulation 4.2(g) is critical to facilitating fair and open access to the NPP facility, while at the same time minimising any possible risks to the integrity and safety of the system.

Consistent with international standards set out in the Bank of International Settlements' 'Principles for Financial Market Infrastructures' (**BIS Principles**), the basic principle underpinning NPPA's eligibility criteria is that payment arrangements should allow for '*fair and open access to services...based on reasonable risk-related participation requirements*'.¹⁸ The BIS Principles further prescribe that '*An FMI should ensure that its participants and any linked FMIs have the requisite operational capacity, financial resources, legal powers and risk-management expertise to prevent unacceptable risk exposure for the FMI and other participants*'.¹⁹ The 'operational capacity' requirement is characterised in the BIS Principles as including reasonable criteria relating to the

¹⁸ p.101, at para 3.18.1.

¹⁹ p.101, at para 3.18.1.

participant's ability and readiness (for example, its IT capabilities) to use an FMI's services.

In this context, the requirement that participants that are (or intend to become) members have 'sound and secure' business practices and operations is a reasonable risk-based request, and uses terminology well understood (and commonly used) in the context of payment systems regulation. That is, 'sound and secure' – as expressly qualified in the relevant regulations - means the participant will not adversely affect the integrity, security, efficiency, reliability or stability of the NPP 'basic infrastructure'. These requirements provide and facilitate the creation of a risk-management framework tailored to address the risks which the NPP could face in the future, while at the same time ensuring the safety and efficiency of the NPP in the present.

Further, as outlined at 3.2(c) above, there are strong safeguards in place to ensure that the NPPA's eligibility criteria will not be applied in a manner that disadvantages prospective NPPA members. The requirement that NPPA provides reasons and a right to review for any adverse decision highlights the transparency and accountability of the decision making process. In addition, the presence of regulatory oversight, in the form of an RBA representative, on the NPPA Board serves to consolidate the existing balances and checks in place.

(b) Licensing - Requirement to be an ADI

The NPP's layered architecture (comprising 'basic infrastructure' plus overlay services) is underpinned by the principle of fair and open access, with the Regulations ensuring that a broad range of ADI and non-ADI participants are able to use the facility via a range of flexible participation options.

Consistent with the RTPC proposal approved by the RBA in 2013, the NPP's 'basic infrastructure' is designed to support real-time account to account payment services, based on certain 'core' functions. In order to deliver these core functions, certain capabilities are essential, including:

- a capability, on a close 24 by 7 basis, to initiate and receive a fast credit transfer between customer accounts;
- a capability to support a separate payment scheme or service which is able to connect to the clearing utility to coordinate transaction activity amongst ADIs; and
- a capability to identify an account at another ADI as the destination for a credit transfer, using addressing information about the payee other than the account number (such as a mobile phone number),

(Core Functions).²⁰

As an incident to the performance of the first Core Function, NPP Participants must be able to manage 'contingency settlement risk' which accumulates if clearing continues during a scheduled or unscheduled FSS unavailability, as contemplated by Part 7 of the NPP Regulations.

As an incident to the performance of the third Core Function listed above, a core component of, and capability within, the NPP is the secure, access-controlled addressing service which supports payment initiation by a payer to a payee using payee addressing

²⁰ Strategic Review of Innovation in the Payments System : Real-Time Payments Committee Proposed Way Forward, (<http://www.apca.com.au/docs/real-time-payments/real-time-payments-proposal.pdf>) p.12-13

information (such as the payee's mobile phone number). NPP Participants who access this service must be able to satisfy the highest standards of information security and systems security. The NPP error and fraud liability framework established by the NPP Regulations obliges the NPP Participant responsible for the registration of payees' account details and addressing information in the addressing service to indemnify other participants and parties against losses resulting from failure to comply with registration standards and requirements (such as, failures in relation to account holder identification, verification and registration errors).

A participant that is not an ADI, and that is not prudentially supervised, would not have, or be able to provide the requisite level of counterparty assurance that it has, the technical, operational or legal capability to perform the Core Functions or manage contingency settlement risk, data security or fraud risks and meet associated liabilities.

However, it is important to note that the design of the NPP does not contemplate that participation is solely limited to those that can perform the Core Functions or meet the potential liability obligations. As noted above, corporates (which connect to the platform as Connected Institutions) and Overlay Service Providers are not subject to the ADI Requirement. As recognised by the RBA, the separation of the 'basic infrastructure' from overlay services promotes flexibility, competition and innovation in the public interest, and facilitates open access to entrants who wish to deliver services on the NPP to end-users in the absence of the capacity to deliver the Core Functions.²¹

Thus, NPPA submits that there is a strong rationale for including the ADI requirement for some participants in the NPP, but this requirement is not excessive and indeed it does not apply to those wanting to provide new services via, or connect to, the platform as Overlay Service Providers or as Connected Institutions. The limited application of the requirement therefore ensures that the NPP is open and will facilitate the provision of services by non-banks and other service providers.

4 Suspension and termination

4.1 Market feedback

The Commission has received feedback suggesting that the suspension and termination provisions give NPPA broad powers. For example, Regulation 9.2(a)(vi)²² contains undefined terms 'contrary to the interest of' and 'adversely affect', which could potentially be construed broadly to restrict participation in the NPP by new entrants (including NPP Participants, Connected Institutions or Overlay Service Providers).

4.2 Background

Under Regulation 9.2, the NPPA Board may suspend an NPP Participant, Connected Institution or Overlay Service Provider for a specified or indefinite period of time where the NPP Participant, Connected Institution or Overlay Service Provider:

- is subject to prudential supervision, and the relevant supervisor requests such suspension;

²¹ Strategic Review of Innovation in the Payments System : Real-Time Payments Committee Proposed Way Forward, (<http://www.apca.com.au/docs/real-time-payments/real-time-payments-proposal.pdf>) p.10

²² Which states that the Board may suspend a member if the member engages in conduct reasonably regarded by the Board to be contrary to the interests of NPPA or which may adversely affect the NPP Basic Infrastructure.

- by agreement with the NPP Participant, Connected Institution or Overlay Service Provider;
- if the relevant NPP Participant, Connected Institution or Overlay Service Provider no longer satisfies the participation requirements set out in Part 4 of the Regulations (i.e. the eligibility requirements);
- if the relevant NPP Participant, Connected Institution or Overlay Service Provider breaches its obligations under the Regulations or Procedures and fails to rectify the breach or provide an explanation of its conduct satisfactory to the Board within 30 business days of a Board request to rectify the breach or provide such an explanation;
- an insolvency event occurs in respect of the NPP Participant, Connected Institution or Overlay Service Provider; and
- if the NPP Participant, Connected Institution or Overlay Service Provider concerned engages in conduct reasonably regarded by the Board to be contrary to the interests of NPPA or which may adversely affect the NPP 'basic infrastructure'.

4.3 Response to feedback

NPPA rejects any suggestion that the proposed suspension provisions under Part 9 are overly broad. On the contrary, the provisions are reasonable and indeed necessary to maintain the integrity, security and viability of the NPP system. NPPA notes that Regulation 9.2 is only triggered upon the incidence of an event which may affect the integrity of the NPP facility (e.g. participant no longer meeting participation requirements, insolvency, or a request by the relevant prudential supervisor for suspension) or by agreement with the relevant NPP Participant, Connected Institution or Overlay Service Provider.

We further note that NPPA's ability to suspend or terminate a participant is a 'last resort' mechanism, which is considered critical in payment system architecture to ensure a payment system can maintain integrity and avoid systemic failure (even in circumstances where one or more participants in the system are unwilling or unable to meet their obligations to other participants). These are not provisions that any Board would apply lightly, as their very application (even if justified) would have severe repercussions for consumer confidence in the system. Similar provisions in other domestic clearing systems administered by APCA, for example, have never been used.

The provisions are also consistent with best international practice. For example, the BIS Principles provide:

*'An FMI should monitor compliance with its participation requirements on an ongoing basis and have clearly defined and publicly disclosed procedures for facilitating the suspension and orderly exit of a participant that breaches, or no longer meets, the participation requirements.'*²³

Further, NPPA submits that, as stated at para 6.1 to Annexure 2 of the Application, the suspension and termination provision in the final paragraph of regulation 9.2 is intended to operate similarly to those included in the APCA's existing clearing system regulations and previously approved by the ACCC. This provision is deliberately general to ensure the Board has flexibility to respond to unanticipated malicious conduct and to protect the minimum performance of the distributed infrastructure. This provision is intended to cover

²³ 'Principles for financial market infrastructures' (April 2012) p103-104 at 3.18.8

a range of unanticipated malicious acts, omissions and conduct (such as for example, spamming, denial of service attacks, and misuse of the assets (such as using the addressing service for deanonymising personal data, ie as a reverse telephone-directory)).

NPPA also notes that in August 2015, the ACCC accepted an APCA suspension provision worded to include the phrase 'contrary to the interests of', considering that the provision did 'not place unreasonable requirements on members' and constituted a 'limited circumstance' in which the suspension provision could be invoked.²⁴ NPPA submits that the wording of 'adversely affect' is comparable in breadth to 'contrary to the interest of'. As such, NPPA submits that both phrases are drafted with sufficient specificity to limit the scope of the Board powers while at the same time retaining a degree of flexibility that would be necessary if an event requiring suspension or termination took place.

5 Participants' relationships with third parties

5.1 Market feedback

The submissions argue that the NPP Regulations should expressly contemplate the existence of relationships between an NPP Participant and a non-NPP Participant third party which delivers services on the NPP, where the NPP Participant may enable NPP access to the third party. In particular, the submissions argue that parties which potentially deliver services on the NPP but are not NPP Participants should have an appropriate level of visibility into and access to decision-making processes that NPPA implements.

5.2 Background

The NPP Regulations provide for different types of participation, including NPP Participants, Overlay Service Providers and Connected Institutions, as outlined at 2.2(d)(ii) above.

5.3 Response to feedback

NPPA has been designed to have appropriate governance arrangements that ensure the company is able to operate and meet its objectives efficiently and effectively. Thus, the Board has been structured to ensure there is appropriate representation for:

- those that have invested in the company and have committed to participate as shareholders;
- the relevant regulator; and
- industry.

The NPP arrangements have been structured in contemplation of proprietary third party contractual relationships without seeking to proscribe them or prescribe their features²⁵. NPPA submits that the structure described above, and discussed elsewhere in this submission, will allow industry and third party stakeholders to have adequate levels of visibility and transparency. The governance arrangements also allow for appropriate

²⁴ ACCC Final Determination: <http://registers.accc.gov.au/content/index.phtml/itemId/1186378/fromItemId/401858>

²⁵ 'Identified Institutions' are financial institutions and corporates with an allocated BSB (for corporates, a sponsoring ADI may dedicate one of its BSBs on a proprietary basis), whose payment messages are traceable using the information uploaded to the Business Reference Data Tables, and required to be handled on their behalf by the NPP Participant who clears/settles for them.

levels of flexibility so broader industry consultation can be implemented as needed (eg, in the form of specific industry working groups or stakeholder forums).

NPPA expects the market for 'sponsored' access to the NPP to be highly competitive. From launch of the NPP, approximately sixty financial institutions (ADIs and corporates) will connect to the NPP via a number of NPP Participants whose business models are focused on providing agency services. NPPA also understands that a number of NPP Participants offering agency solutions to the market also expect to provide indirect NPP connection solutions to corporate customers enabling them to have practical use of all of the technical functionality available to NPP Participant. As enhanced ICS functionality becomes available (for example, the ICS payment request), it is likely that many NPP Participants will be active providers of agency solutions, including third party payment initiation services. The competitiveness of the market for sponsored access is expected to provide discipline in the provision of information by NPP Participants to third parties, and thereby promote transparency.

The NPPA website will host information (including the NPP Regulations and the public version of NPP Procedures²⁶) relevant to third parties and stakeholders in the NPP and will include links to relevant external information sources.

NPPA also submits that the RBA's right to appoint a director and, from the time the NPP becomes operational, an observer on the Board, or indeed a permanent right of appointment (as described in section 2.2(f)(iii)), will provide regulatory oversight and allow representation of broader public policy objectives (and thus of broader stakeholders) directly into the decision-making processes of the Board.

Finally, NPPA notes that the RBA has broad powers under the *Reserve Bank Act 1959* and the *Payment Systems (Regulation) Act 1998* directed to the efficiency, competition in, and stability of, payment systems. To the extent the arrangements established by the NPP Regulations fail to deliver expected public policy objectives, the RBA may be expected to exercise its regulatory powers.

6 Costs incurred by participants

6.1 Market feedback

The ACCC has received feedback suggesting that the requirement in provision 4.2(d)²⁷ could be onerous for NPP Participants in the early stage of business development or with little capital and may constitute a barrier to entry with the effect of excluding new innovations and/or participants.

6.2 Background

(a) Initial funding

[REDACTED]

A prospective NPP Participant is required to be a member and subscribe for shares in NPPA to provide the level of capital funding which is commensurate with its size, market capitalisation and significance in the Australian payments system (ie as either a 'medium'

²⁶ Confidential information (including technical, operational and security standards and requirements detailed in the NPP Procedures) will be redacted from public version of all materials on the NPPA website but is available to prospective participants under non-disclosure agreement.

²⁷ Whereby NPP Participants agree to pay all fees, costs, charges and expenses which may be levied on, or which are to be reimbursed by, NPP Participants in accordance with the NPP Regulations.

or 'low' band member) and which is equivalent to the funding contributed to date by each other NPP Participant in the same governance band. [REDACTED]

However, in considering costs, it is important to note that in addition to this direct investment, each NPP Participant has incurred substantial costs in building the back office capability to integrate core banking IT systems with the NPP. It has been estimated that collective costs incurred by NPPA's 13 members will reach \$1 billion by October 2017.

In addition, the NPP Regulations contemplate the collection by NPPA of fees from some or all NPP Participants, Connected Institutions or Overlay Services Providers, including the fees outlined in further detail at section (b) below to defray its operating costs, including annual charges payable to SWIFT for the operation of the NPP.

NPPA's publicly available strategic blueprint positions the infrastructure as *economically self-sustaining (not profit-maximising)*²⁸.

(b) Ongoing funding

From October 2019, NPPA's costs of operating the NPP are intended to be defrayed entirely by transaction fees. Regulation 4.2(d) requires that prospective NPP Participants agree to pay all fees, costs, charges and expenses which may be levied on, or which are to be reimbursed, by NPP Participants in accordance with the NPP Regulations.

Regulation 3.1(c) provides for NPPA to charge participants the following:

- charges payable by NPP Participants and Connected Institutions only:
 - transaction fees;
 - fees for NPP componentry (i.e. the software, hardware and other services provided by NPPA to establish connectivity to the NPP)²⁹; and
 - addressing service usage fees;
- charges payable by NPP Participant applicants and Overlay Service Provider applicants only:
 - application fee payable by an applicant upon lodgement of a participation application; and
- charges payable by NPP Participants, Connected Institutions and Overlay Service Providers:
 - annual administration fees in relation to the general costs and expenses of managing and operating the NPP 'basic infrastructure'.
 - any applicable fee in the event dispute resolution takes place.

²⁸ <http://www.nppa.com.au/what-is-the-npp/frequently-asked-questions/>

²⁹ The share subscription made by an NPP Participant satisfies its obligation to pay for a standard-sized 'kit' of NPP componentry; payment is required for any additional componentry the Participant may elect to provision. Fees for NPP Componentry 'kits' apply to Connected Institutions which do not subscribe for shares in NPPA.

6.3 Response to feedback

NPPA is funded privately and it needs to be financially viable in order to be able to operate. As such, fees and charges need to be levied in order to cover the company's ongoing operations costs. These are directed towards covering the costs of operation rather than maximising profit. That said, as outlined above, the company offers a variety of fee structures depending on the degree of participation required.

At the same time, participants in the NPP must have a degree of financial viability to be able to operate. Enterprises with no finance or those that cannot afford to pay for the basic infrastructure they need to operate may not be best placed to offer payment services (no matter how innovative) as they could create material risks for consumers relying on them. In this context, having sufficient funds to be able to afford paying for the basic infrastructure that a business will need in order to provide its services (such as the NPP) is not an anti-competitive barrier to entry but rather a necessary condition to be a viable commercial enterprise in the first place.

Section 5.3 of this submission also outlines a range of alternative mechanisms by which interested parties may connect to the NPP via agency solutions provided by an NPP Participant, enabling them to either defray or avoid costs which might be levied on them directly as an NPP Participant.

In that context, NPPA submits that the fee structure and alternative access mechanisms outlined above provide an adequate balance in terms of securing the financial viability of the business while at the same time ensuring that fees and charges are not excessive and do not create unnecessary or anti-competitive barriers to entry.

7 Conclusions

The NPP facility, as an industry project, gives effect to the RTPC Proposal which set out a 'path forward' for real-time payments infrastructure in Australia and which was accepted by the RBA's Payments System Board in February 2013. NPPA's member ADIs have furthered the RBA's and industry's common objectives by financing, building, and facilitating open access to the NPP facility by parties including:

- Participant ADIs, who have funded the NPP facility and are able to connect to it for clearing and settlement ;
- Other ADIs, the majority of whom by number have chosen to connect to the NPP indirectly via agency services provided by another Participant;
- consumers, businesses and governments, who are able to use the payment services offered via the NPP facility; and
- non-ADIs, which benefit from NPPA's governance framework that enables access for Overlay Service Providers and corporates wishing to offer or experience innovative payment solutions .

Accordingly, NPPA notes the broad public benefits which NPPA delivers to participants by balancing principles of open access with the requisite balances and checks to ensure the security and integrity of a facility that is required to deliver the Core Functions (described in section 3.3(b)).

NPPA considers that the views expressed in market feedback do not raise any competition concerns. Specifically, NPPA notes:

- the Board already ensures appropriate representation. In particular, the presence of independent directors and regulatory oversight on the Board ensures that broader policy and stakeholder interests are considered, and that Board decisions are subject to the existing (and appropriate) balances and checks in place. Any concerns in relation to conflicts of interests are ill-informed and unfounded;
- NPPA's governance arrangements have been structured to avoid and manage any conflict of interests, are clear and well understood, and allow for adequate levels of visibility and transparency to industry and third party stakeholders, as well as flexibility so broader industry consultation can be implemented as needed;
- existing eligibility and licensing requirements, financial contribution requirements as well as suspension and termination provisions are reasonable and indeed necessary to maintain the viability (and integrity) of the NPP system and the operations of NPPA. Many of the requirements and provisions are consistent with best international practice and designed to retain a degree of flexibility to enable NPPA to address any serious issues that may arise. The NPP has also been designed to facilitate the provision of services by non-banks and other service providers, to promote flexibility, competition and innovation in the public interest.

The concerns raised in submissions are not in relation to the provisions which are the subject of the authorisation application. Rather, they are largely concerned with the general development and operations of NPP itself, which have been the subject of extensive consultation with industry and regulatory authorities over a number of years. They therefore do not raise relevant, if any, public detriments, and in any case, any public detriments would be far outweighed by the public benefits of the NPP (as set out in the Application).