The price of disloyalty

Why competition has failed to lower ATM fees

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Josh Fear

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Summary

One of the most expensive ways for Australians to access their own money is by using an automatic teller machine (ATM) that is not provided by their own bank. In most cases, third-party ATMs charge $2 for every transaction, including checking one's account balance. In other words, $2 is the price consumers pay every time they are 'disloyal' to their bank.

In April 2009, the Reserve Bank of Australia (RBA) put in place a package of reforms to the ATM system. The reforms ensured that customers would be charged directly by ATM owners, rather than being charged indirectly through their financial institution as in the past. The new rules also required that ATMs display the cost before customers confirm the transaction. One of the stated objectives of the reforms was to place 'downward pressure on the cost of ATM withdrawals'. To date, however, third-party ATM fees typically remain at $2 or higher. In the RBA's words, the $2 fee has become a 'benchmark'.

There is substantial public opposition to ATM fees. Survey results indicate that the great majority of Australians (82%) believe it is unfair for banks to charge $2 to use their ATMs. Survey findings also corroborate the Reserve Bank's claim that consumers have changed their behaviour in order to avoid paying third-party ATM fees now that they are more aware that such fees exist.

In the year following the 2009 reforms, the use of third-party ATMs fell 18 per cent, delivering consumers savings of some $120 million. But because ATM fees typically remain at $2, virtually all these savings stem from behaviour change on the part of consumers rather than lower prices, even though behaviour change was never an explicit objective of the RBA's reforms. Altogether Australians are still paying an estimated $753 million per year on third-party ATM fees.

The increased transparency of ATM fees may have led to another form of behaviour change which is not necessarily in the best interests of consumers. Two in three survey respondents (66%) reported paying for purchases with a credit card to avoid ATM fees, but a substantial minority (18%) do so without then paying off their credit card in full. These people then end up paying high rates of interest on their purchases, effectively negating any savings they might have made on ATM fees and in the process delivering additional revenue to credit card providers. The perception that using credit cards can help reduce ATM fees may therefore serve to exacerbate the problems with personal debt that many Australians experience.

Survey results also show that young people bear a disproportionate burden of ATM fees. One in four survey respondents (26%) reported paying a $2 ATM fee at least once in the past week, but some 40% of those aged between 18 and 24 years paid an ATM fee. People under the age of 25 typically earn less than those who have been in the workforce for longer, meaning that ATM fees would constitute a much higher proportion of income for younger people than for other ATM users. Given that the use of third-party ATMs declines with age it is possible that children with a bank account are also paying a higher than average share of ATM fees. Similarly, people on low incomes are likely to pay more in ATM fees as a proportion of their incomes than people who are financially better off.

Although reforms to the ATM system have not led to lower prices across the board, they have resulted in other changes. The effective abolition of indirect fees (known as 'interchange fees') has meant that owning ATMs is now a much more profitable endeavour than it used to be. The number of ATMs available to consumers has grown strongly since the reforms. In fact, the provision of ATMs is now so profitable that rents for ATM sites have been rising, and investors can now 'buy' one or more ATMs in return for a guaranteed revenue stream.

A further change is that the profits associated with fees charged by ATM owners have shifted from banks whose customers used the most third-party ATMs to those organisations which can attract the highest number of 'foreign' customers to their ATMs – that is, those that own the largest ATM fleets. This is because ATM owners can now charged much more for the same service as in the past. Even though interchange fees of $1 were sufficient to ensure ATMs were widely available prior to 2009, virtually all ATM owners now charge double that amount or more.

In addition to promoting competition and lowering prices, the reforms to the ATM system were intended to ensure that ATM owners had sufficient financial incentive to maintain and add to the existing ATM stock, and this has undoubtedly come to pass. Studies by the RBA and ACCC have shown that the cost of providing ATM services is typically well below $1 per transaction.

With such a lucrative revenue stream, ATM providers as a group appear to be reluctant to 'break ranks' by competing on price. With ATM fees more transparent than in the past but by no means fully transparent, there is no 'first-mover advantage' for ATM owners looking to gain more customers by lowering their prices. And with the RBA's statements demonstrating a conviction that the recent reforms have 'worked', consumers are likely to continue paying $2 every time they use an ATM from a bank which is not their own for the foreseeable future.

Policy options

There are several options open to policy-makers looking to ensure that Australian consumers are charged a fair price for using ATMs.

First, regulators could require that ATM owners display the cost of foreign-bank transactions prominently on the outside of their machines, so that potential users can see at a glance what they would be charged if they used that ATM. This would mean that cardholders do not need to reach the 'point of no return' before the cost of the transaction is displayed. In this way, ATM fees would become as transparent as petrol prices are for people driving past a service station. Such a requirement would mimic what market forces appear to have delivered in some other countries, such as in the United Kingdom and the Netherlands, but have failed to generate in this country.

Second, fees for balance enquiries should be abolished entirely. Such fees serve to discourage responsible financial behaviour by effectively doubling the cost of ATM fees for cardholders who wish to know how much money is in their account before withdrawing cash. Once an ATM is in place the cost for the ATM provider of a balance enquiry is negligible, since no cash handling needs to take place. With both banks and government agreeing that it is a priority to encourage greater financial literacy, there is a strong case for removing fees on balance enquiries altogether.

Third, investigation of the actual costs of providing ATM services could be undertaken by an appropriate government body (such as the RBA or the ACCC) regularly and as a matter of course. To date, such research has been carried out on an ad hoc basis, but regular information would allow the public and regulators to determine whether the gap between the costs of providing ATMs and the revenue this can generate is appropriate or excessive. Research should consider the potential savings that ATMs can bring for financial institutions in the form of reduced staffing costs, as well as the differential costs of providing ATMs in areas which may be comparatively costly to service. In addition, research should also investigate the extent to which different population groups, including people in low-income households, Indigenous people and children, are paying third-party ATM fees.

The fourth option available to policy-makers is the most interventionist, but may be necessary if price competition does not emerge in the ATM market in the near future in order to prevent the exploitation of consumers by ATM owners. Capping foreign-ATM prices at a level which is above what would apply in a perfectly competitive market (that is, reflecting the actual costs of providing ATM services plus a reasonable return) would ensure that Australian consumers are not overcharged. Price caps could be contingent on certain criteria (for example, location type) rather than uniformly applied, but they should be based on an independent assessment of the true costs of providing ATMs as determined by an independent regulator such as the ACCC. At the very least, price controls could apply in locations where only one ATM is available, since such ATMs enjoy a local monopoly. Alternatively, a uniform price cap could be applied but a subsidy provided to operators who are prepared to deploy ATMs in less convenient locations, in the same way that the Government subsidises telephone services in rural and regional areas.

Introduction

Each and every day millions of Australians pay financial institutions to access their own money. Some pay more while others pay less, depending on the way they go about getting their hands on their money. Sometimes, as with interchange fees on EFTPOS transactions, the price consumers pay for their own money is largely invisible, being factored into the prices of goods and services charged by retailers. In other cases, the cost of using your own money is embedded in bank fees, or else in forgone interest from transaction accounts with negligible rates of interest.

One of the most expensive ways for Australians to access their own money is by using a third-party automatic teller machine - that is, as ATM not provided by their own bank. In most cases, third-party ATMs charge $2 for every transaction, including checking one's account balance. In other words, $2 is the price consumers pay every time they are 'disloyal' to their bank. In the year to October 2010, Australians paid a total of $642 million in fees on third-party ATM cash withdrawals, plus millions more to check their account balances.[1]

Of course, someone has to pay for the infrastructure that gives people access to their own money. The modern electronic payments system is a wonder of speed and convenience, allowing people to avoid queuing up in a bank branch to withdraw money. It is entirely justifiable for the providers of payment infrastructure to charge money to use it. *How much* they charge is a different question. In contrast with Australia, in nations such as the United Kingdom and the Netherlands free third-party ATMs are widely available.[2]

This paper investigates why Australians continue to pay such a high price for disloyalty, and whether it is fair that they should do so. It explains the way that ATM fees are regulated, and questions whether recent reforms have been successful in giving consumers the best deal. It also describes what consumers think about ATM fees, and how they behave as a result. The paper concludes with a consideration of the options available to policy-makers looking to bring down ATM fees.

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[1] Official RBA statistics indicate that Australians made around 320,808,917 foreign-bank ATM withdrawals in the year to October 2010. If these transactions were made at an average cost of $2, this equates to $641,617,834 in ATM fees. By contrast, information recently provided by Treasury to the Senate includes an estimate of $540 million in fees on ATM withdrawals in the year to March 2010. However, these figures do not include balance enquiries, meaning the real figure is likely to exceed $642 million. Because RBA statistics refer to the number and value of withdrawals but not the cost of fees, the effect of ATM operators charging less or more than $2 per withdrawal is impossible to gauge. However, as noted later in this report, a $2 withdrawal fee remains the standard price. Sources: Reserve Bank of Australia 2010, *Statistical Tables – ATM Cash Withdrawals*, Table C4, December; Senate Economics References Committee Inquiry into Competition in the Australian Banking Sector, *Treasury Response to Question on Notice – ATM Fees*, Transcript 13 December 2010 (E47).

[2] In the UK 57% of around 58,000 ATMs are free of charge to any customer. Typically these free machines are found in locations attracting a high volume of transactions such as in bank branches. Interchange fee are paid by the customer's bank. Charging ATMs handle only around 5% of withdrawals, revealing a strong consumer preference for free withdrawals. In 2009, the UK government, industry and consumer groups agreed on a scheme of financial support for cash machine operators to expand into low-income areas, which by June 2009 resulted in the installation of an additional 601 free cash machines serving 1.5 million consumers. Sources: <http://www.link.co.uk/Media/NewsReleases/Pages/600thnewfreecashmachinegoesliveinlow-incomearea.aspx> ATM Working Group 2006. *Cash Machines – Meeting Consumer Needs*. <http://webarchive.nationalarchives.gov.uk/+/http://www.hm-treasury.gov.uk/d/atm_working_group_final.pdf>

The regulation of ATM fees

Like many in the business sector, financial institutions in Australia are vocal in their opposition to government regulation. But despite the liberalisation of Australia's financial sector in the 1980s, there are many areas of financial activity that remain subject to tight regulation, both to discourage excessive risk-taking and to promote competition.

One of the ways in which the financial sector is regulated is through the payments system. The Reserve Bank of Australia defines the payments system as those 'arrangements which allow consumers, businesses and other organisations to transfer funds usually held in an account at a financial institution to one another. It includes the payment instruments – cash, cheques and electronic funds transfers which customers use to make payments – and the usually unseen arrangements that ensure that funds move from accounts at one financial institution to another.'[3]

The network of ATMs around Australia is one element of the payments system and therefore subject to regulatory oversight. Indeed, the financial sector itself, through the Australian Payments Clearing Association (APCA) has asked government to ensure that the payments system is properly regulated. According to the RBA, the 'APCA … came to the view in late 2008 that the most effective way of providing legal certainty … was through regulation by the [Reserve] Bank.'[4] Such a position stands in stark contrast to the statements of individual banks about the need for ongoing deregulation of the financial marketplace.

Recent reforms

Prior to 2009, Australian consumers did not pay a *direct* fee when they used a third-party ATM. Instead, their financial institution paid the owner of the ATM an 'interchange fee'; this was then passed onto customers in the form of a 'foreign fee' sometime after the transaction. Interchange fees were usually set at $1 per transaction; foreign fees, by contrast, ranged between $1.50 and $2.10 per transaction, but were typically set at $2.[5]

For consumers, there were two problems with this situation. First, and perhaps most important, was the lack of information about the true cost of using a foreign-bank ATM at the time of making the transaction. Foreign fees would appear on someone's bank statement weeks or months later; this was the only way people would know with certainty that they had been charged such a fee.

The second problem was the roundabout way in which fees were charged. Instead of charging consumers directly for using an ATM, financial institutions paid an interchange fee to the ATM owner and then recovered these costs from their customers. However, there was a gap between the interchange fee (typically $1) and the foreign fee (typically $2). In other words, financial institutions tended to make money from this arrangement – usually $1 per transaction. With some 407 million foreign-ATM withdrawals made in the year 2008, this delivered financial institutions an additional $407 million in annual revenue purely as a result of the gap between foreign fees and interchange fees.[6] This arrangement was largely hidden from consumers;

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[3] Reserve Bank of Australia 2011. 'About the Payments System', <http://www.rba.gov.au/payments-system/about.html> accessed 2 Feb 2011.

[4] Reserve Bank of Australia 2009. *An Access Regime for the ATM System*, February, p.5.

[5] Reserve Bank of Australia 2009.

[6] In 2008, there were a total of 865,848,760 cash withdrawals from ATMs, and 458,548,301 withdrawals from 'own' ATMs. This means that 407,300,459 cash withdrawals were made from foreign ATMs in that year. If each transaction delivered an average of $1 to financial institutions (in the form of the gap between the foreign fee and the interchange fee), this corresponds to some $407 million. This figure is likely to be an underestimate, because it does not include balance enquiries, which also attract a fee at foreign ATMs.

interchange fees were not mentioned on bank statements and agreements between financial institutions and ATM owners were not revealed publicly. Perversely, it was in the interests of financial institutions for their customers to use ATMs that were not their own, because this would generate a revenue stream that would not result from customers using their own ATMs.

In recognition of these and other problems with the ATM system, the Reserve Bank of Australia introduced new rules to regulate the ATM system in March 2009. The reforms prohibited the charging of interchange fees (except in certain limited circumstances), and allowed ATM owners to charge consumers directly at the time of transaction. The new rules also required ATMs to display the cost of the transaction and give customers an opportunity to cancel it if they do not wish to proceed. The RBA believed that these changes would 'make the cost of cash withdrawals more transparent to cardholders and place downward pressure on the cost of ATM withdrawals' and 'promote competition between financial institutions'.[7]

In reforming the ATM system, the RBA was also concerned about 'a significant risk that the number of ATMs in Australia will decline over time, as non-bank owners of ATMs find it unprofitable to deploy and service machines.'[8] With interchange fees normally set in bilateral agreements between banks and ATM owners at $1, the RBA believed that the cost of providing ATMs would eventually exceed the revenue that ATMs could generate, at which point it would not be in the interests of ATM owners to continue operating or deploying ATMs. The RBA also identified various barriers to entry to the ATM 'market', with current players able to prevent new entrants from competing on even terms.[9] It predicted that its reforms would 'help to ensure continued widespread availability of ATMs by creating incentives to deploy them in a wide variety of locations, providing consumers with choice and convenience.'[10] In other words, according to the RBA the provision of ATMs needs to be a sufficiently profitable endeavour that the number of ATMs increases rather than declines over time.

The consequences of reform

According to the RBA, the reforms to the regulation of ATM fees have 'been meeting their objectives.'[11] In support of this claim is that the fact that the number of foreign-ATM withdrawals fell by 18 per cent over the first year the changes were in place (see Figure 1), with such transactions falling from 44 per cent to 38 per cent of all ATM withdrawals. The RBA also reports that consumers have been withdrawing more money per transaction 'so that they visit foreign ATMs less often.' In the year following the reforms, the average value of foreign-ATM withdrawals rose from $148 to $156, the number of balance enquiries fell by more than half, and EFTPOS cash withdrawals grew by 9 per cent. As a result, consumers paid around $120 million less in foreign-ATM fees compared with the year before the changes were made. As the RBA puts it, the reforms have 'resulted in cardholders changing their behaviour in order to reduce the fees that they pay.'[12]

Source: Reserve Bank of Australia 2010, *Statistical Tables – ATM Cash Withdrawals*, Table C4, December. <http://www.rba.gov.au/statistics/tables/index.html>

7 Reserve Bank of Australia 2011.

8 Reserve Bank of Australia 2009, p. 1.

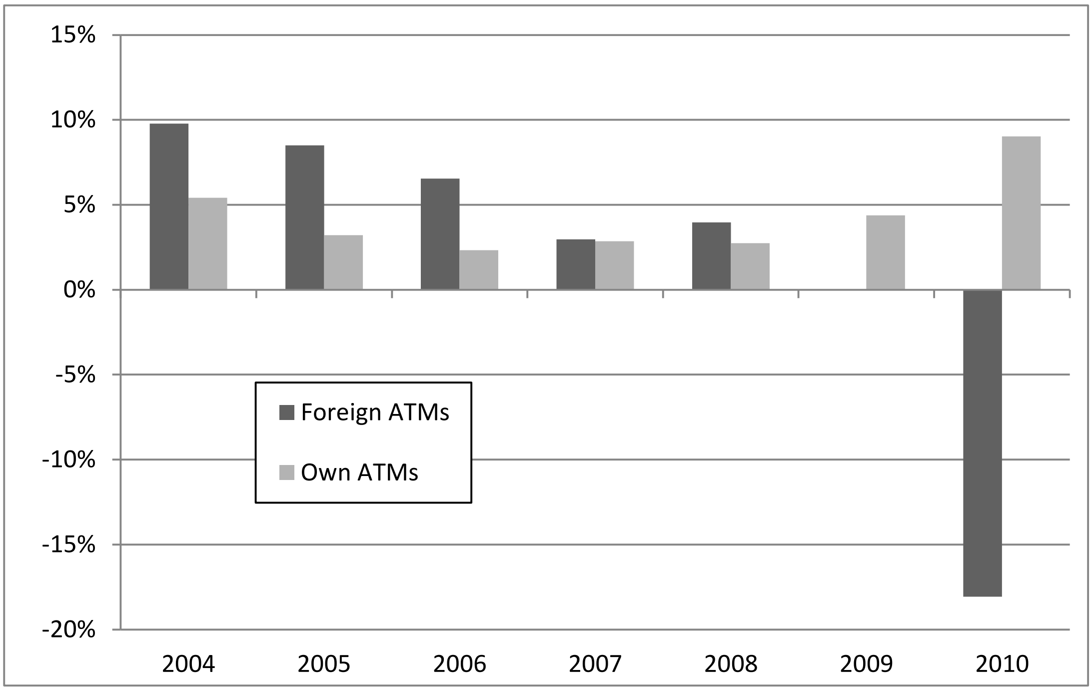
9 Reserve Bank of Australia 2009.

10 Reserve Bank of Australia 2011.

11 Filipovski, B. and Flood, D. 2010. *Reform of the ATM System – One Year On*, RBA Bulletin, June Quarter, Reserve Bank of Australia.

12 Filipovski and Flood 2010.

Figure 1: Percentage change in the number of ATM cash withdrawals by ATM type (year to February)



Source: Reserve Bank of Australia 2010, *Statistical Tables – ATM Cash Withdrawals*, Table C4, December.

In fact, behaviour change is the chief reason why consumers are now spending less on ATM fees than in the past, even though the RBA did not explicitly articulate its desire for behaviour change when it put the reforms in place. Instead, it emphasised the need for competition to place 'downward pressure on ATM fees.'[13] Unfortunately, competition has largely failed to lower prices. The standard price for foreign-ATM withdrawals remains at $2; only one of the big four banks, the National Australia Bank, has lowered its price (to $1.50) and most other providers charge $2 or more.[14] As the RBA puts it, 'the $2 foreign fee that applied prior to the reforms has established a benchmark' and 'relatively little price competition among ATM owners appears to have developed to date'.[15] A small number of ATM providers have lowered their prices for balance enquiries, but in most cases a balance enquiry costs the same as a cash withdrawal.[16]

Although price competition remains absent for the time being, the RBA has identified another area where the reforms have been successful: in encouraging providers to deploy more ATMs. The number of ATMs has reportedly grown by some 1,500, or around 6 per cent, with approximately half of the additional ATMs being provided by financial institutions and half by independent owners. The provision of ATMs is now so profitable that rents for ATM sites have risen,[17] and some entrepreneurs have taken the opportunity to 'sell' ATMs to investors.[18] With

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13 Reserve Bank of Australia 2009.

14 In a minority of cases, balance enquiries at foreign ATMs now attract a lower fee than in the past. The RBA notes that such transactions 'do not incur the costs associated with cash handling [and] are cheaper to provide than ATM withdrawals.' Source: Filipovski, B. and Flood, D. 2010.

15 Filipovski, B. and Flood, D. 2010.

16 Filipovski, B. and Flood, D. 2010.

17 Filipovski, B. and Flood, D. 2010.

direct charges of $2 per transaction, rather than interchange fees at $1 as in the past, operating an ATM can now deliver twice the revenue per transaction. This has meant that ATM numbers have been increasing even in areas that are less profitable, 'including in rural, regional and remote areas … [and] relatively low-usage locations and temporary ATMs at public events.'[19]

In December 2010, the Gillard Government announced a series of initiatives to promote a 'competitive and sustainable banking system'. One element of this package was the establishment of a joint Treasury/RBA Taskforce to investigate 'the need for further action to enhance implementation of ATM reforms introduced in March 2009 to boost competition and transparency.' The Taskforce will also deliver a separate report on 'issues specifically affecting Australian Indigenous and other remote communities in relation to ATMs.'[20]

Survey of ATM users

To explore community attitudes and behaviour in relation to ATM fees, the Australia Institute conducted an online survey of 1,294 Australians in November 2010. The survey sample was representative of the adult Australian population by age and gender.[21]

The great majority of survey respondents (82%) said that it is *unfair* for other banks to charge $2 to use their ATMs, while only 15% said it was *fair*. As Table 1 shows, customers of credit unions and smaller banks were more likely to believe that ATM fees were unfair than customers of big four banks.

Table 1: Do you think it is fair for other banks to charge you $2 to use their ATMs?

	Big 4 customers	Customers of other banks	Customers of credit unions	All
Yes, it is fair	17%	13%	13%	15%
No, it is unfair	80%	86%	85%	82%
Not sure	3%	1%	1%	2%
Total	100%	100%	100%	100%

Base = 1,294. Question wording: 'Currently, if you use an ATM that is not from your own bank you are likely to be charged $2 for withdrawing money or checking your balance. Do you think it is fair for other banks to charge you $2 to use their ATMs?'

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[18] For example, Own Your Own ATM Pty Ltd offers investors a chance to invest in different kinds of ATMs (eg a 'Level One ATM' or a 'Business Hours ATM') with a guaranteed rate of return. See <http://www.ownyourownatm.com.au/index.html>.

[19] Filipovski, B. and Flood, D. 2010.

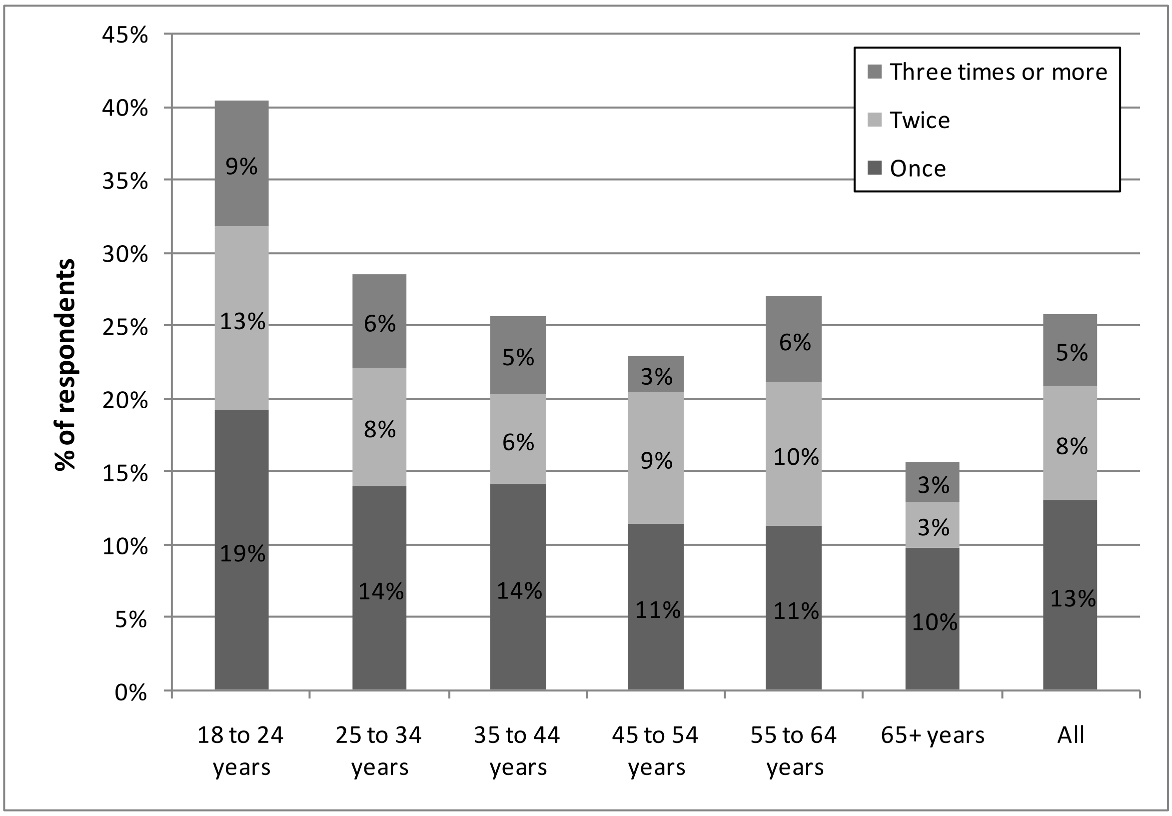
[20] Commonwealth of Australia 2010. *Competitive and Sustainable Banking System*, Australian Government, December. <http://www.treasury.gov.au/banking/content/default.asp>

[21] Survey respondents were sourced from an independent online panel provider, and provided with a small incentive to encourage participation ($2). To ensure a representative sample, quotas were applied by age, gender and state/territory, and data was post-weighted by age and gender.

One in four respondents (26%) said that in the past week they had been charged a $2 fee for using an ATM from another bank. This included 13% who reported being charged $2 once in the past week, 8% who reported being charged $2 twice and 5% who said they had been charged three times or more.

Young people are disproportionately likely to use foreign-bank ATMs: 40% of respondents aged between 18 and 24 years reported paying a $2 ATM fee in the past week. By contrast, only 15% of people over 65 said they had paid an ATM fee. People living in rural locations were also more likely to report paying a $2 ATM fee (29%, as compared with 25% of people in metropolitan locations). Meanwhile, people in low-income households were noticeably less likely to pay a $2 ATM fee (22%, compared with 27% of those in middle- and high-income households)[22], presumably because a $2 fee has a greater impact on household budgets for those on lower incomes.

Figure 2: Proportion of respondents who paid a $2 foreign-bank ATM fee in the past week



Base = 1,256. Includes respondents who indicated whether they had paid a $2 foreign-bank ATM fee in the past week.

The vast majority of respondents (93%) said they knew the location of the nearest ATM from their own bank to their home. This indicates that most Australians are now sufficiently aware of

[22] For the purposes of this paper, low-income households are defined as households with a combined income before tax of less than $40,000 per annum. Middle-income households have a combined income of between $40,000 and $80,000, and high-income households have a combined income of more than $80,000. These three categories each correspond to roughly one-third of all households in Australia.

the ATM fees that they have taken the trouble to find out how to avoid them in the normal course of their lives. However, it is likely that the bulk of third-party ATM fees are incurred at times when consumers are away from home or are otherwise unable to find an ATM from their own bank. The small proportion of respondents who said they did not know where the nearest ATM is were more likely to have paid a $2 ATM fee in the past week (36%, as compared with 25% of those who did know where the nearest ATM is).

Survey respondents were asked whether they did various things in order to avoid or minimise paying a $2 ATM fee. Four in five respondents (82%) said that they only ever use their own bank's ATMs – although a slightly lower figure (76%) said they had not paid a $2 ATM fee in the past week. This suggests that many people try to avoid foreign-bank ATMs, but they do not always succeed.

Around two in three respondents (69%) said they withdraw cash as part of EFTPOS transactions in order to avoid paying an ATM fee, while a similar proportion (66%) said they pay for purchases with a credit card. Clear gender differences emerged in this respect: women were more likely than men to withdraw cash via EFTPOS (75% compared with 63%), while men were more likely than women to pay with a credit card (69% as against 62%).

One in two respondents (50%) said that they make larger withdrawals but less often in order to avoid or minimise paying a $2 ATM fee. A much smaller proportion (20%) said that they take out a large amount of cash *when using another bank's ATM*.

Table 2: Do you do any of the following to avoid or minimising paying a $2 ATM fee?

	Male	Female	All
Only ever use your own bank's ATMs	83%	80%	82%
Withdraw cash as part of EFTPOS transactions	63%	75%	69%
Pay for purchases with a credit card	69%	62%	66%
Make larger withdrawals but less often	49%	50%	50%
Take out a large amount of cash when using another bank's ATM	21%	20%	20%

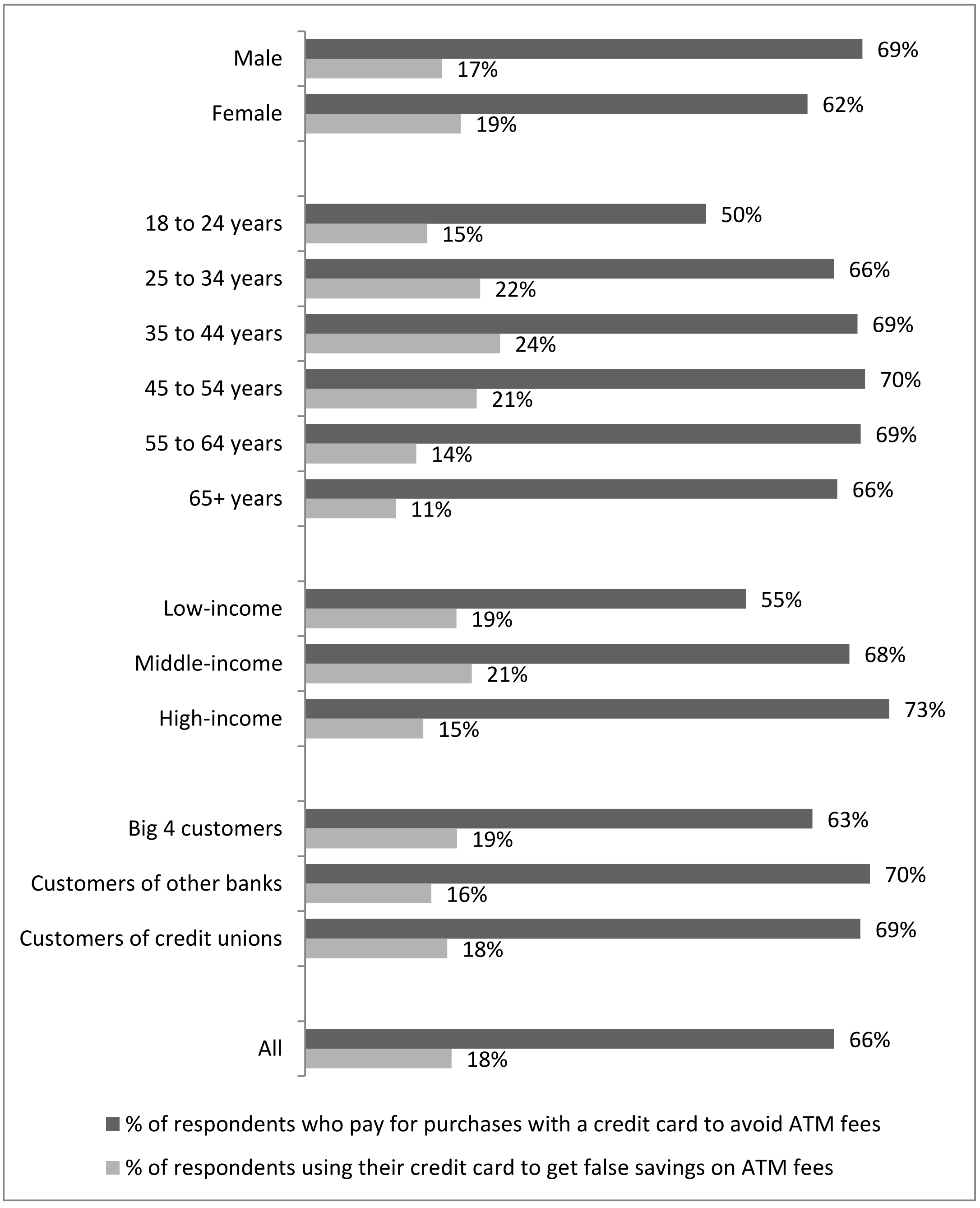
Base = 1,294

Paying for purchases with a credit card in order to avoid ATM fees makes sense if people then pay off their credit card in full each month. If they do not pay off their credit card in full, any savings they make in ATM fees are likely to be outweighed by the additional interest they pay on their credit card purchases. Among the two-thirds of respondents who reported paying by credit card to avoid ATM fees, some 28% reported not paying off their credit card in full. Put another way, 18% of people pay for purchases with a credit card with the express purpose of avoiding ATM fees, and subsequently pay high rates of interest on those purchases.

As Figure 3 shows, even though men are more likely to make purchases on their credit card in order to avoid ATM fees, women are more likely to make *false savings* because they do not subsequently pay off their credit card in full. Such false savings are much less common among young adults (probably because fewer young people have a credit card) and among people older than 65; the proportion of people making false savings in this way is highest among those aged 35-44 years (24%).

The proportion of people who make credit card purchases to avoid ATM fees rises with income; three-quarters of those in high-income households do this. However, those in high-income households are less likely to make false savings, because they pay off their credit card in full more often.

Figure 3: False savings on ATM fees by using credit card



Base = 1,294.

Implications

Survey results corroborate the Reserve Bank's claim that consumers have changed their behaviour in order to avoid paying foreign-bank ATM fees in the wake of reforms to make such fees more transparent. Four in five respondents (82%) said that they only ever use their own bank's ATMs to avoid paying a $2 fee, while a majority of people reported doing other things, such as withdrawing cash with an EFTPOS transaction (69%) or paying for purchases with a credit card (66%), to avoid ATM fees. Such behaviour relies on consumers knowing that they will be charged if they use foreign-bank ATM, but it is also driven by a belief that ATM fees are not legitimate. The great majority of survey respondents (82%) said that it is 'unfair' for other banks to charge $2 to use their ATMs.

Consumers have changed their habits to the extent that they are avoiding 18 per cent of the fees they were charged prior to the 2009 reforms, but they are still paying high ATM fees the remaining 82 per cent of the time. Survey respondents spent an average of $0.84 in the past week on foreign-bank ATM fees; this corresponds to $43.68 each per year. This means that altogether Australians are paying around $753 million per year in foreign-bank ATM fees.[23] This is consistent with RBA figures showing that fees on foreign-ATM withdrawals (but excluding balance enquiries) correspond to around $642 million per annum.

Of further concern is that the burden of ATM fees is distributed unevenly across the population. One in four survey respondents (26%) reported paying a $2 ATM fee at least once in the past week, but some 40% of those aged between 18 and 24 years paid an ATM fee. Indeed, one in ten young people (9%) said they had done so three or more times in the past week. The survey sample did not include respondents aged younger than 18 years, but given that the use of foreign-bank ATMs declines with age it is possible that children with a bank account are also paying a larger than average share of ATM fees. People under the age of 25 typically earn less than those who have been in the workforce for longer, meaning that ATM fees would constitute a much higher proportion of income for younger people than for other ATM users. For people on lower incomes more generally, ATM fees are also likely to represent a higher proportion of spending than for people who are financially better off.

While consumer behaviour has been changing in the wake of reform, ATM owners have not changed their own practices by competing on price as was predicted by the RBA. The $2 foreign-ATM fee remains a 'benchmark'; although some ATM owners deviate from this price the great majority of ATMs still charge $2. Part of the explanation for the failure of the reforms to lower prices stems from the way that the information given to consumers about the cost of ATM withdrawals is 'embedded' in the transaction rather than being apparent before the transaction is started, as with (say) a petrol station advertising its prices to motorists. The rules do not require that ATM owners advertise their prices prominently before a transaction is initiated - only that customers are given an opportunity to withdraw once the price is revealed. In the mind of a ATM user looking to 'shop around' on price, information about the cost of using a foreign-bank ATM simply comes too late to be of practical use. The RBA expects this situation to change in the future:

> An obvious response is for ATM owners with a low direct charge to advertise the charge prominently so as to attract additional throughput and higher fee revenue. There is nothing to prevent owners from doing this, although the strategy requires the general public to understand

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[23] As at June 2010 there were 17,229,344 people over the age of 18 in Australia. If each adult spent an average of $43.68 on ATM fees each year, this corresponds to a total annual expenditure of $752,577,746. Note that this does not include amounts spent by people under the age of 18 on ATM fees; the survey sample was restricted to people aged 18 and over. Source: ABS 2010. *Australian Demographic Statistics*, Cat No. 3101.0, June.

> pricing sufficiently to react accordingly. To date, advertising of prices has occurred only in isolated cases, but this and other competitive strategies might develop over time as the market matures.[24]

Instead of bringing down prices, the reforms to the ATM system put in place in 2009 have actually meant that owning an ATM is now even more profitable than it was prior to the reforms. Independent operators can now expect to generate twice as much revenue from the same number of transactions because of the effective removal of interchange fees imposed by financial institutions on ATM operators. The sudden jump in the profitability of ATM ownership has meant that the number of ATMs has increased, rents for ATM sites have risen, and opportunities to invest in individual ATMs have even emerged. To date, the benefits of reform have accrued exclusively to ATM owners, and particularly to owners which can attract many 'foreign' users – except where consumers have avoided using foreign ATMs altogether. Virtually no ATM operators charge $1 per withdrawal, even though the $1 interchange fees that applied in the past provided sufficient revenue to ensure ATMs were widely available prior to 2009. This is despite the RBA explicitly stating that the purpose of its reforms was to place 'downward pressure on the cost of ATM withdrawals'.

For financial institutions, the abolition of interchange fees removed a large source of revenue. In the past most banks charged their customers $2 per transaction in foreign fees but paid only $1 in interchange fees to ATM owners, meaning they received an extra $1 every time a customer used a foreign-bank ATM. Since March 2009 it is no longer in a bank's financial interest for their customers to use other ATMs, although it is of course highly profitable for customers of other banks to use their ATMs. In fact, banks now typically generate double the revenue that they used to when people who are not their own customers make a withdrawal or balance enquiry at an ATM that they own.

Curiously, banks appear to be recouping some of the losses they may have incurred as a result of the abolition of interchange fees via another form of behaviour change on the part of consumers. Two in three survey respondents (66%) reported paying for purchases with a credit card to avoid ATM fees, but a substantial minority (18%) do so without then paying off their credit card in full. These people then end up paying high rates of interest on their purchases, effectively negating any savings they might have made on ATM fees and in the process delivering additional revenue to credit card providers. Put simply, banks appear to have recouped some of their losses (and perhaps even made additional revenue) through an increase in the interest they charge on credit card purchases.

The finding that 18% of Australians make 'false' savings on ATM fees by sometimes purchasing on credit and not regularly paying off their debts in full reflects the broader tendency for consumers to act in ways that are not always consistent with their own financial best interests. In fact, there are many ways in which financial decision-making deviates from what would be considered purely 'rational' behaviour, to the point that such behaviour is the exception rather than the norm. A considerable proportion of Australians are perpetually 'playing catch-up' by carrying a credit card debt from one month to the next.[25] The perception that using credit cards can help reduce ATM fees may therefore serve to exacerbate the problems with personal debt that many Australians experience.

It should be emphasised that for financial institutions (as opposed to independent operators) the cost of providing ATMs must be offset against the supposed cost savings associated with customers making transactions through ATMs rather than in a bank branch. The drive to reduce

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[24] Filipovski, B. and Flood, D. 2010..

[25] Citi Australia 2010. *Evidence versus Emotion: How do we really make financial decisions?* Prepared by the Australia Institute, December. <http://www.citi.com.au/citigroup/pdf/Citi_Fin_Report_full_document.pdf>

staffing costs was one of the principal reasons why banks encouraged customers to use ATMs when they were first introduced. This may be one reason why banks are prepared to operate ATMs at below the standard price in certain limited circumstances. For example, as at May 2010 Westpac operated one ATM in a remote area of the Northern Territory which charged 50 cents for withdrawals and 25 cents for balance enquiries.[26] But competitive forces have not compelled banks to lower their prices across the board, because the vast majority of ATMs operated by financial institutions charge four times this amount. A study by the RBA in 2007 found that the weighted-average cost of an ATM withdrawal is 74 cents and the median cost 85 cents – less than half of the standard fee both before and after the reforms.[27]

While the RBA's goal of promoting competition between ATM providers is an admirable one, it should be noted that all ATMs exist in a particular physical location and therefore can potentially take advantage of a local monopoly. Even if prices were fully transparent to consumers before using an ATM (which they are currently not), in many cases there is only one ATM in a given location. The nearest alternative ATM may be within walking distance, in the next suburb, or even hundreds of kilometres away. The further away an alternative ATM is, the less any competitive pressures can be expected to apply.

Nowhere is this more of a problem than in remote Indigenous communities. As a report by the Australian Financial Counselling & Credit Reform Association (AFCCRA) makes clear, people in these communities have no choice but to use the ATM in their location. Such ATMs are usually deployed by independent operators rather than financial institutions, and sometimes charge more than $2 per transaction; indeed, an ATM in one community charges $10 per transaction. AFCCRA's study found that 'ATM fees of $20-$40 are commonly incurred by people on the day Centrelink payments are due. As well, Indigenous consumers are more likely to withdraw small amounts of cash and so incur more fees.'[28]

Compared with remote Indigenous communities, the problems stemming from local monopolies on ATM services are less pressing in urban areas, where there may be enough consumer traffic to warrant multiple ATMs or EFTPOS outlets within walking distance of one another. Nevertheless, even if a cheaper ATM is 'just around the corner' consumers may not necessarily be aware that this is the case. Moreover, because ATM services are to some extent a substitute for other forms of electronic banking services (such as EFTPOS), it is also possible for a given ATM to have a local monopoly over the *type of service* as well as the ATM service. Again, this is likely to present more of a problem in regional and remote areas, but factors such as time of day and the availability of internet access can contribute to ATM providers having an effective local monopoly over the type of service that consumers can access.

In the future, technology may be able to assist in helping consumers locate the cheapest ATM in a given location. For example, software developers and/or financial institutions may develop smartphone applications that inform users where to find the cheapest ATM (just as some financial institutions already have applications telling consumers where the nearest own-bank ATM is). This may help to bring about more price competition among ATM owners, but such an eventuality would of course depend on consumers already owning the right device to make use of these kinds of applications.

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26 The fact that all the major banks were willing to waive their ATM fees for two weeks in flood-affected areas of Queensland is further evidence that banks are able to lower their ATM fees if they perceive it to be in their interests to do so. Source: *The Age* 2011. 'Banks waive ATM fees in Queensland flood zones', *The Age*, 15 January. <http://www.theage.com.au/national/banks-waive-atm-fees-in-qld-flood-zones-20110114-19rch.html>

27 Reserve Bank of Australia 2009.

28 Australian Financial Counselling & Credit Reform Association 2010. *ATM Fees in Indigenous Communities*, November, p.3.

Most ATM operators continue to charge the same amount for balance enquiries as for cash withdrawals. Clearly the actual costs to operators of a balance enquiry is substantially less than the cost of a withdrawal (because no cash handling is required), and in a competitive market prices would reflect this difference. With prices for withdrawals and balance enquiries remaining largely the same, it would seem that competition has not delivered any benefits for consumers beyond the savings that they have made by deliberately avoiding foreign-bank ATMs.

In many cases consumers can be charged ATM fees twice if they first check their account balance and then withdraw cash. In this situation, the cost of a balance enquiry is effectively $4 (unless someone then decides not to take out any cash, perhaps because they have insufficient funds). This 'double-whammy' in fact serves as a penalty for financial responsible behaviour. Many consumers rely on automatic direct debit payments for certain bills, and need to ensure that they have sufficient funds in their account to meet those commitments. If they do not do so, they may then be subject to penalty fees (or, as banks refer to them, 'exemption fees') for breaching their direct debit payment schedule. By charging $4 for checking account balances before they withdraw cash, foreign-ATM providers discourage consumers from being aware of their current financial situation. This not only increases the chance of people not meeting their financial commitments (and perhaps being charged highly profitable penalty fees), it also is in direct contradiction to the stated goals of the all the major banks and government to promote greater financial literacy in the Australian population. For example, according to the Australian Bankers' Association, 'We need to ensure that all Australians can understand how to behave with their finances, manage their money, increase their savings, make good investment decisions, manage their debt and understand how to behave with their spending.'[29] Excessive fees on balance enquiries clearly undermine such ambitions.

Conclusions

Reforms to the ATM system in 2009 have resulted in several notable changes. First, consumers are now much more aware of the costs of using an ATM from a bank that is not their own, and some people have changed their behaviour to avoid using foreign-bank ATMs. This has delivered consumers an overall saving of around $120 million.

Second, the effective abolition of interchange fees has meant that owning ATMs is now a much more profitable endeavour than it used to be. The number of ATMs available to consumers has grown strongly since the reforms; the extra machines have been provided by financial institutions and by independent operators in roughly equal measure. This includes additional ATMs in less convenient locations, such as rural and regional areas.

Third, the profits associated with fees charged by ATM owners have shifted from banks whose customers used the most foreign ATMs (because these banks benefited most from the large gap between interchange fees and foreign fees) to those organisations which can attract the highest number of 'foreign' customers to their ATMs – that is, those that own the largest ATM fleets.

Fourth, changes to the regulation of ATM fees mean that it is no longer in the interests of financial institutions for their customers to use ATMs from other providers. Because they can charge cardholders directly, ATM owners – whether banks or independent operators – will now profit whenever someone uses an ATM and incurs a fee.

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[29] Australian Bankers' Association 2011. 'Financial Literacy Info Centre' <http://www.bankers.asn.au/Default.aspx?ArticleID=1003>, accessed 11 February 2011.

Despite these changes, the reforms have not delivered what would have been an unambiguous sign of success from a consumer perspective: lower prices for using a foreign-bank ATM. Instead, ATM providers have kept prices artificially inflated, typically at $2 per transaction. It is possible that the current pricing regime is simply a relic of the former situation, in which a $2 fee was standard. This is the RBA's view, and it expects prices to fall once the market matures (although when this will take place is unclear).

An alternative explanation is that ATM providers currently derive such a lucrative revenue stream that as a group they are reluctant to 'break ranks' by competing on price. With ATM fees more transparent than in the past but by no means fully transparent, there is no 'first-mover advantage' for ATM owners looking to gain more customers by lowering their prices. One of the principal advantages of a market is price discovery, but continuing high profit margins show that this particular market-based reform has not succeeded. Instead, the ATM market has 'discovered' that the price of using foreign ATMs is exactly the same as in the past; it is only the distribution of profit between the different owners of ATMs that has changed.

Moreover, two of the principal objectives of the recent reforms to the ATM system remain in conflict. The RBA continues to rely on competition to lower prices at the same time as it relies on relatively high prices to encourage owners to deploy additional ATMs. The reforms were intended to ensure that ATM owners had sufficient financial incentive to maintain and add to the existing ATM stock, and this has undoubtedly come to pass. The typical fee of $2 is well in excess of the cost of providing the service; while such costs may rise over time it is inconceivable that they will approach $2 anytime soon. But with the RBA's statements demonstrating a conviction that the recent reforms have 'worked', consumers are likely to continue paying $2 every time they use an ATM from a bank which is not their own for the foreseeable future.

Policy options

There are several options open to policy-makers looking to ensure that Australian consumers are charged a fair price for using ATMs.

First, regulators could require that ATM owners display the cost of foreign-bank transactions prominently on the outside of their machines, so that potential users can see at a glance what they would be charged if they used that ATM. This would mean that cardholders do not need to reach the 'point of no return' before the cost of the transaction is displayed. In this way, ATM fees would become as transparent as petrol prices are for people driving past a service station. Such a requirement would mimic what market forces appear to have delivered in some other countries, such as in the United Kingdom and the Netherlands, but have failed to generate in this country.

Second, fees for balance enquiries should be abolished entirely. Such fees serve to discourage responsible financial behaviour by effectively doubling the cost of ATM fees for cardholders who wish to know how much money is in their account before withdrawing cash. Once an ATM is in place the cost for the ATM provider of a balance enquiry is negligible, since no cash handling needs to take place. With both banks and government agreeing that it is a priority to encourage greater financial literacy, there is a strong case for removing fees on balance enquiries altogether.

Third, investigation of the actual costs of providing ATM services could be undertaken by an appropriate government body (such as the RBA or the ACCC) regularly and as a matter of course. To date, such research has been carried out on an ad hoc basis, but regular information would allow the public and regulators to determine whether the gap between the costs of providing ATMs and the revenue this can generate is appropriate or excessive. Research should consider the potential savings that ATMs can bring for financial institutions in the form of reduced staffing costs, as well as the differential costs of providing ATMs in areas which may be comparatively costly to service. In addition, research should also investigate the extent to which different population groups, including people in low-income households, Indigenous people and children, are paying third-party ATM fees.

The fourth option available to policy-makers is the most interventionist, but may be necessary if price competition does not emerge in the ATM market in the near future in order to prevent the exploitation of consumers by ATM owners. Capping foreign-ATM prices at a level which is above what would apply in a perfectly competitive market (that is, reflecting the actual costs of providing ATM services plus a reasonable return) would ensure that Australian consumers are not overcharged. Price caps could be contingent on certain criteria (for example, location type) rather than uniformly applied, but they should be based on an independent assessment of the true costs of providing ATMs as determined by an independent regulator such as the ACCC. At the very least, price controls could apply in locations where only one ATM is available, since such ATMs enjoy a local monopoly. Alternatively, a uniform price cap could be applied but a subsidy provided to operators who are prepared to deploy ATMs in less convenient locations, in the same way that the Government subsidises telephone services in rural and regional areas.

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