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COMPETITION COMMISSION

SUBMISSION ON THE BANKING ENQUIRY

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CONTENTS

Introduction to the NET 1 UEPS functionality.

Anomalies and archaic banking practices in South Africa.

The future of South African Banking

Conclusion.



1. Introduction to the NET 1 UEPS functionality

Net1 have developed the UEPS (Universal Electronic Payment System) that makes use of the patented FTS (Funds Transfer System) methodology to provide a fully integrated payment, switching and settlement system suitable for multiple applications and services, meeting the requirements of the un-banked and under-banked populations.

The Net 1 payment system enables customers to effect transactions “off-line” in underdeveloped areas where traditional financial institutions and their services have limited penetration or are otherwise unavailable due to the lack of, or limited branch, Automated Teller Machines (or “ATM”), POS, support and communications infrastructures.

All transactions effected through the UEPS occur between 2 (two) cards at a POS rather than through a host mainframe (as with traditional banking and payment systems), since all of the relevant information necessary to perform a financial transaction is held on the smart cards, inclusive of the funds available of the transacting cardholders. The transfer of value between the cards accordingly can take place without any communication with an on-line host mainframe as all validations; audit trails, encryption, decryption and authorization take place or are generated between the cards themselves.

- **AFFORDABILITY**, as most of the transaction costs are borne by the organizations that make use of the channel and there are minimal monthly fixed fees payable by the cardholders;
- **SECURITY**, since the card serves as a substitute for cash, but provides loss tolerance which protects the card holder in the event of loss or stolen cards; and
- **SIMPLICITY**, as a biometric fingerprint identification system is used by the cardholder to access the card and perform transactions.



Anomalies and archaic banking practices in South Africa

2. Anomalies and archaic banking practises in South Africa

An assumption that there is a **complex monopoly** in the South African banking arena and the National Payment System is probably correct. Many of the “standard” banking practices are set up specifically in a way to allow Banks to charge extraordinary transaction and administrative fees. As a non-bank player in the Financial Services field, Net 1 is aware of these and shares the frustrations of many other similar institutions in South Africa. The statements and questions under this heading will justify the fact that people in the **lower income** bracket (LSM 1-4) actually foot the bill for the mentioned fees.

2.1 Acquiring

2.1.1 The rules for “branded” cards must be clear and should apply across the board.

- i.e. – VISA
- MASTERCARD
 - AMEX, etc.

2.1.2 Member banks must have transparent procedures with regard to:

- Costs }
- Technology } -- These should be indicated by product
- Risk }

Clear indication must be given as to WHO bears the risk, as the cost factor could be influenced, with clear distinction between debit and credit transactions.

2.1.3 Rules are unilaterally laid down for merchants.

- Single acquiring promotes the routing of a transaction via Bankserve to Issuing Banks with the fee implication linked to it.
- Multiple acquiring could result in a fee of approximately 0.45%. This is a far cry from the fees charged currently. The reasons for the “sort at source” issue could be seen as an eye blind to protect charges.
- Discounting cash transactions is not allowed – why? The poorer part of the population pays with cash. Should they be penalized because of the “system”?
- Point of Sale devices belong to the bank. Another source of income for the bank. Why can the merchant not own the POS device?



- 3rd party acquirers can switch directly to the Issuing Banks. This will eliminate the extra costs and will create an opportunity for healthy climate of competition at these acquirers.

2.1.4 Rules of the banks for non-branded cards.

- Why are these rules different?
- What is the process of approval, by whom and how long does it take?
- How are fees for non-bank cards such as store cards, loyalty cards, etc. determined?

2.1.5 It is not clear how the Banks justify the acquiring fee.

2.1.6 Multiple Acquiring should be legitimized. There is technology available to allow one POS device to actually communicate with several Issuers. This will result in a huge saving. Maybe this is the reason that the Banks do not wish to allow it?

2.2 Issuing

2.2.1 It necessary to ask: who and on what basis is the interchange fee is decided? This must apply for debit and credit transactions.

2.2.2 A debit reduces the interchange fee, but then the card holder is charged – resulting in the poorer paying the fees instead of the merchant.

2.2.3 Credit card fees are paid by the cash payers (poorer segment) who pay the same as the card holders.

2.2.4 Why not have a local branded card outside VISA/Matercard at much lower cost and outside their rules.

2.2.5 The new rule to have a pin instead of a signature (back of card) places the risk on the card holder instead of the bank, as there is now no proof that the card holder did not initiate the transaction.

2.2.6 Why should the local population pay for the International interoperability?

2.2.7 VISA / Mastercard limit the POS devices to their standards. Why? There are much more functionality such as pre-paid utilities, etc. that could be accommodated.

2.2.8 Retailers are prevented to utilize the POS device for their own purpose or from introducing new products. Maybe it is because the bank will not receive a share? These devices can definitely accommodate additional software without prejudice to the bank's software.



2.3 Other areas to be investigated

- 2.3.1 The fee for a rejected debit order ranges between R100.00 and R150.00. This amount will be deducted as “arrears” before anything else when there is another credit on the account. Some debit card accounts are put into negative balances. The cost to the bank for such a rejected transaction is approximately R4.50!
- 2.3.2 The EDO (AEDOS and NAEDOS) facility is being developed for the Micro Finance industry, Insurance companies and other institutions with the need to get an “early morning” deduction. Unfortunately there are some flaws:
- Single acquiring is enforced with the cost implication as mentioned.
 - It seems that the fee will be much higher than the 4.5% of a normal debit card transaction. Why? Will unsuccessful transactions be levied and if so, why?
 - Limited access to accounts – none on credit cards, Mzansi accounts, etc.
 - Banks are supposed to also submit their “on-us” transactions into the EDO pool to be randomized. Will this happen or will they find a way to bypass the system?
 - The EDO system is aimed at lower income groups. Deductions for the thousands of weekly paid people cannot be accommodated as the debit orders will only run a day later and this will result in a “no funds available” situation.
- 2.3.3 Collusion with regards to price fixing is a very sensitive subject.
- 2.3.4 The PAYMENT ASSOCIATION of SOUTH AFRICA (PASA) is a regulatory institution reporting to the SARB.
- Does PASA have the authority to sanction any of the member banks?
 - Where does the funding for this body originate?
- 2.3.5 Internationally, multiple acquiring by third parties is an acceptable norm. The approximate cost seems to be .25 of a percent or less.
- 2.3.5 A few years ago, Boland Bank attempted to launch a “Mini ATM” project. The major banks did not approve and the project was declared “illegal”. Currently one of the “big four” is running with such a project. Why?



CONCLUSION

The biggest part of the population operates in the second economy in this country. However, they are the ones with the least access to banking services. Their right to accessible, cost effective and functional banking services cannot be denied. We believe that the NET 1 model is the key to successful BANKING and TRANSACTING in South Africa.

There are numerous other flaws and obvious shortcomings in the South African banking and payments arena and the company would gladly enter into further discussions with the panel in this regard.

The opportunity to present to the panel on 30 November 2006 in Pretoria is appreciated.



