



**The Institute for Public Sector Accountability**  
*'res ipsa loquitur'*

## **House of Commons – Finance Committee -ATM Fees Brief-**

**April 2007**

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## **Executive Summary**

Amid glowing reports by all Canadian banks of large increases in profits, accompanied by large executive salary increases, comes a claim to have ATM fees examined and reined in. Such a move will show that the government seems to be willing to interfere with the market. Generally, Canadian bank charges and service fees have relatively been higher than those of American banks. The reason for this is not usually widely discussed, and Canadian customers seem to only get some help, if any, when bank profits go up or when it becomes politically advantageous to do so. The real problem is that the Canadian banking industry operates as a virtual oligopoly. With few banks and little competition, the industry can charge whatever it likes, and as is the case for fewer and fewer services, especially in rural areas.

Furthermore, the issue of ATM fees may not be very well understood by the general public. While banks have closed many branches and reduced face-to-face contact with their customers, they have also increased the use of electronic banking and provided more ATMs. As they decrease brick and mortar service delivery, banks have cut costs and charged more for their services, thus resulting in part to the higher profits. However, a vast majority of ATMs are not operated by Banks, but are in fact the property of smaller institutions and private owners. Therefore to attack only the banks for the increase in ATM fees is a little bit disingenuous.

We do not defend the banks, but we do not believe that the government should interfere in the operations of the market. Instead if the government wanted to reduce the costs of banking services they could very easily do so. The government has the power to legislate how the banks operate. A free-market philosophy approach should look at allowing bank mergers, but with an important caveat – allow the entry of more foreign banks in the Canadian market.

Should both mergers and foreign banks entry in the market be allowed, we believe that the following will happen:

- There will be increased competition due to more banks in the market place
- Fees will come down and perhaps in some cases such as in the United States disappear
- Customers will find themselves with more outlets to do their banking face-to-face
- For those who lose their jobs, they could be absorbed by new foreign bank outlets.
- More importantly larger Canadian banks resulting from the mergers will become more able to compete in the international arena. Such a move would benefit all concerned - reduced fees, make Canadian banks more competitive, and open the banking industry to more competition.

## Introduction

The Institute is dedicated to present the facts to enable the public to make an informed decision. We therefore take this opportunity to present our point of view on the issue of ATM fees and ask the committee to refrain from setting any new regulations based solely on the fact that banks are making too much profit.

As soon as the Canadian banks released their profits of \$19 billion for 2006, there has been a call for regulating ATM fees. The premise is that charging the customer an average fee of \$1.50 for an ATM transaction on the Interac system is tantamount to 'double dipping'. While the demand for reform of ATM fees is not confined to Canada, forcing Canadian banks to abandon this fee may be based on the wrong assumptions.

The use of ATMs came into being with new technology, and as we find new ways of accessing bank accounts it is more likely that the number of ATM will decrease and not increase. While it is a popular means of accessing one's money it does not mean that regulating the fees today will either increase its usage or reduce banks revenues. We must remember that the use of ATM is by choice and that it is a convenience rather than a service that all customers **must** use because they do not have any other alternative to access their money.

Looking at the Canadian market we must also examine the number of machines in use and who actually operates them. Besides we must also compare fees and how these fees are actually collected. To make an assumption that increasing bank revenues are a result of ATM fees, and that they should therefore be regulated would be wrong. The fact remains that the use of ATM is still a choice and voluntary, any new regulation will only be that - new rules and no real gain for the consumer.

If we are so concerned about bank charges and fees we should take a remedial approach which promotes more competition in the industry instead of more regulations. The Canadian banking system needs a complete overhaul to allow for banks to provide more services, such as insurance, and also allow for more foreign banks to enter the market and compete on a level playing field. Mergers and acquisitions within the Canadian industry should be allowed to make Canadian banks bigger and more competitive in the international arena. By the same token allowing foreign banks to fully operate in the Canadian market will increase domestic competition and lower service fees, as the apparent oligopoly disappears.

## Background

According to Retail Banking Research Ltd., There are over 1.5 million ATMs installed around the world, with a new one being installed every 5 minutes. However, with the advent of new technology, the continued growth may well be stunted soon. For the time being, ATMs are still a convenience resulting from one of the most revolutionary technological inventions of the twentieth century. It provides millions of people with the convenience of accessing their money on a 24 hour basis at home or when travelling abroad. Most banks provide a list of their machines' location and can be viewed on the internet.

Canadians have embraced the use of ATM more than most other nations. There may be two reasons for this, one because over the past years we have seen the closure of many local branches, two because we may have the lowest ATM fees of any industrialised country. In 2005, the major banks operated 15,590 machines (see Appendix A). Of the approximate 54,000 ATMs in use in Canada (2006) only 30% of those machines are owned by the major banks. The vast majority of so called 'white label' machines, because they do not have a bank logo, are owned by either smaller institutions or even private operators.

Canadians do not usually pay for the use of ATM transactions if they use a machine operated by their own bank. However if they choose another operator's machine they have to pay a fee. These fees are generally made up of at least two charges:

- "Network access fee" which is charged to use another bank's machine
- "Convenience fee" which is charged by the ATM's operating bank for the use of its machine by the customer of another bank.

The truth is that some banks may waive the network access fee in certain cases where the customer either has an account which covers all access fees or perhaps holds an account with a minimum balance of \$1,000. The convenience fee, on the other hand, is charged for maintenance, and infrastructure investment. In the U.S. and in Britain, in cases where ATM fees seem to be non-existent, they may be charged indirectly as part of a banking package service fee.

ATM fees may also vary, depending on locations. For example, fees in say a private club, or a casino are usually higher. Private operators, through the Interac link, must also pay certain fees for 'partial dispense', which occurs when a machine jams and only dispenses part of the transaction. To link the costs of all ATM operators and conclude that there is automatic gouging may be misleading. The claim that these fees can consume up to 25% of the minimum withdrawal amount of \$20 is only supported by using the highest fee in the range (\$5.15) as a basis for comparison. We should also exclude foreign ATM fee from the calculation.

## Obsolescence and Competition

The answer to the so called 'gouging' is very simple, and does not require any regulation by the government. This issue is a waste of time and any prolonged investigation will only result in a waste of taxpayers money. A regulation of ATM fees is more likely to hurt the small operators rather than reduce the big banks' profits.

In a recent article in the *Economist* magazine of February 2007 entitled 'The End of the Cash Era' ATMs are described as future dinosaurs. In Africa increasingly cell phones are being used as a vehicle for banking transactions. Similarly in industrialised countries the cell phone is being used to pay for such mundane things as parking fees and purchasing of food from dispensing machines. As new technology allows for more integration of cell phones with other services, ATMs will very likely become obsolete. Banks who have a good flair for profits will quickly reduce the number of ATMs and move out of any market with diminishing profitability. Therefore, to regulate ATM fees at this stage can only be characterized as a political move that will not really benefit the consumer.

Banks do not need new regulations for its ATMs fees, but the Canadian Banking industry needs a complete revamp to allow more competition in the domestic market. Many banks are expanding their operations into the global market. Mergers and acquisitions by Canadian banks have taken place in the United States, Latin America, Asia, the Caribbean and some banks are planning to expand their operations in China. From a strategic point of view this will give Canadian banks a competitive advantage and greater presence in the international arena. While these foreign operations generate approximately 30% of the banks' gross revenues, it can also be said that these foreign acquisitions are partly financed by profits generated from Canadian operations. If we think that Canadian service fees are too high we should not regulate them, but we should allow for greater competition in the domestic market. If Canadian banks are expanding globally, Canadian consumers deserve to get the benefits of global competition by allowing foreign banks to compete fully for their business in the domestic market. Refusing to do so seems more like protectionism of the banking industry.

In recent years many small towns and even cities have seen a reduction in the number of branches operated by Canadian Banks. Although some Banks are reconsidering this strategy and plan to open new branches, we must not forget that it will be the same banks and not new institutions that will provide the services. The number of outlets may be increasing but the competition will not. To allow bank mergers by Canadian banks, coupled with the opening of the

market to foreign banks will surely increase competition and thus provide Canadians with more accessibility and result in lower fees. Although new legislation passed in 1999, allowed foreign banks to establish operations in Canada without having to set up Canadian-incorporated subsidiaries, their operations focus on commercial banking and other lending activities. These foreign lending branches are not allowed to take deposits, while full-service branches are only permitted to take deposits greater than \$150,000. The big six banks comprise over 90% of the assets of the Canadian banking sector. It seems that they operate as a virtual oligopoly, without real competition.

## Conclusions

The banking industry is basking in huge profits but **IPSA** takes the view that these positive financial results should not become the reasons for the regulation of ATM fees. The financial results are a combination of a number of factors including growth in the domestic market and foreign operations; they are not a direct result of high ATM fees.

To regulate ATM fees will, in our opinion, be a poor reaction to the wrong problem. In fact as supported by other sources, ATM operations are more likely to decrease rather than increase. Any new regulations would be like imposing a tax on 8-track tapes in a market dominated by CDs and MP3s. The government should follow its own approach used for the telephone industry and allow more competition in the banking industry.

Instead of regulating ATMs we believe that the whole banking industry could benefit from a complete review, which would result in further competition in the industry by relaxing the existing rules to allow foreign banks to fully participate in the Canadian Banking industry. We do not need more regulations; Canadians would prefer lower banking fees generated by greater competition. To quote: "...legislative and regulatory changes have benefited efficiency in Canadian financial services. This shows the importance of removing any remaining restrictions that inhibit competition and efficiency, but provide little (or no) benefit in terms of financial soundness."<sup>1</sup>

We cannot agree more with the above statement from the Bank of Canada, and urge the Finance Committee to look at the issue of ATM fees not in isolation but as part of a bigger picture for a review of the Canadian bank industry.

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<sup>1</sup> Are Canadian Banks Efficient? A Canada U.S. Comparison. Jason Allen (Bank of Canada), Walter Engert (Bank of Canada) and Ying Liu (Université de la Méditerranée) **Bank of Canada December 2006**

## Appendix A

<b>ABMs</b>	<b>Numbers</b>	<b>Period</b>	<b>Institutions</b>	<b>Comments</b>	<b>Source</b>
Bank Owned	15,590	Oct 2005	6 largest Banks, HSBC & Laurentian	Excludes private-label ABMs owned by banks	Canadian Bankers Association
Total ABM	50,649	Dec 2005	Members of Interac		Interac
Transactions per Capita		2004		Canadian transactions include only cash deposits and withdrawals	Bank for International Settlement
<b>Canada</b>	34.6				
<b>France</b>	20.3				
<b>Netherlands</b>	29.7				
<b>Sweden</b>	37.4				



Canada is one of the most democratic countries of the world. Its diversity and cultural richness are the basis for our prosperity. However in recent past there have been too many instances of government mismanagement, which if left unchallenged can and will endanger our democratic system.

In the 21<sup>st</sup> century we can no longer manage our public institutions with 20<sup>th</sup> century models. It is time to re-examine the role of government in our society and seek new ways for the delivery of public services. We need more transparency and accountability in the public sector. There is a need for a new vehicle to allow citizens to express their opinions and provide new ideas to maintain our prosperity.

**The Institute for Public Sector Accountability (IPSA)** is a non-profit organization founded to promote transparency and accountability in the public sector. **IPSA** is dedicated to the enhancement of democracy.

**Vision:**

Through research, analysis, evaluation and the publication of papers and articles, IPSA will inform and provide new ideas and add a new voice to the democratic process.

**Mission:**

- To inform the public on issues related to the public sector
- To be a voice to make government more transparent and accountable
- To educate the public on matters concerning public policy
- To promote dialogue between the public, politicians, and public sector administrators

**How can you help?**

The Institute for Public Sector Accountability is a not-for-profit organization, and we cannot enhance democracy and promote your ideas without your help. We invite you to support us and make a donation. Please contact our President and CEO at (403) 238-3865 for more information.

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