

21 April 2015

Head of Payments Policy Department  
Reserve Bank of Australia  
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CabFare welcomes the Recommendations of the Financial Systems Inquiry with respect to Surcharging on Card Transactions. CabFare supports the thrust of the Inquiry's recommendations on Card Regulation.

In terms of the current consultation by the Reserve Bank on the FSI recommendations relating to Card Surcharging and Interchange Fees we support the need to:

**1. Bring all Credit and Debit Cards within a common regulatory framework.**

There are too many unregulated cards operating in Australia including Cabcharge and Union Pay. This creates technical as well as compliance costs and barriers to an efficient operation of a payment market place. This has the potential to increase costs to Acquirers and Merchants when these cards are incorporated into the mainstream payment system.

**2. RBA to examine the costs of providing card services to the Australian Community.**

Such a review has to tackle what are the reasonable costs of acquiring transactions for a merchant including not only the interchange fees but also the fundamental question of how Merchant Service Fees are set by Card Companies.

CabFare cannot see any justification for maintaining Merchant Fees as a % (ad valorem) of the Transaction Value. These fees are set at different levels for different merchants, and particularly discriminate against small businesses. This approach cannot be justified in an electronic payment ecosystem where the costs of acquisition (or transaction), aside from the Merchant Fee, effectively are fixed.

**3. Restructure Merchant Service Fees from Ad Valorem Pricing to Postage Stamp Pricing**

We make the following observations:

1. The cost to the Card Insurer of servicing its Merchants is common irrespective of the size of the transaction.
2. Card Issuers are using Merchant Fees as a surrogate for lending to the Cardholder. The costs of providing credit are ones that should be borne solely by the cardholder who is obtaining a short-term credit facility.
3. Using a % Merchant Fee forces the Merchant either to recover the cost as a % of each individual card transaction; or to smear the costs across all sales. If the latter approach is chosen, which is the stated corporate policy of both Visa and MasterCard, then those consumers who don't use cards pay for the costs of the credit provided to those consumers who do. In other words it becomes a deadweight loss on the payment system.
4. No matter the approach a Merchant follows poor price signals are sent to consumers.

*Gouging of Merchants by Card Issuers*

The current practice of Ad valorem pricing mechanisms in Merchant Service Fees is clear "gouging" by Card companies of merchants. CabFare's perspective is that setting MSF in this way reflects poor risk and credit management practices in Card Issuers. Card Issuers should not use Merchant Service Fees as a way of subsidising

unsecured credit provision to cardholders. Allocating risk and pricing of credit needs to be the focus of the Card Issuer and not viewing the merchant as a low risk “soft target” to subsidise the Card Issuer’s poor risk management practices.

CabFare’s position is that a flat Merchant Service Fee would:

- i. Make it a simpler and fairer system to all
- ii. Drive down costs to consumers
- iii. Drive down costs to Card Companies.
- iv. Provide Consumers with a simple, easy to understand service fee for using Cards.
- v. Enable the cost of Credit provision to be recovered from the party receiving the credit (i.e. The Cardholder).

*Opening the methodology by which Merchant Service Fees charged by all Card Companies to regulatory scrutiny must be a priority for any comprehensive review by the RBA.*

### **3. Tiered Surcharging.**

The proposals contained in the PSB paper are complex and unnecessary. Implementation will be costly and confusing to merchants and consumers. The need for “tiered surcharging” arises purely because Card Issuers use ad valorem MSF methodologies and they fail to cost recover from Cardholders the full cost of the card’s benefits. Premium Cards are NOT being priced appropriately including so called frequent flyer benefits. These benefits are being cross-subsidised by both Merchants and low value card holders. Premium Cards are marketed as an “entitlement” and “status”. Accordingly full cost recovery of these cards should be directed at the cardholder as beneficiary of the entitlement either via higher card fees or more aggressive interest rates, or elimination of interest free periods; or a combination of these. Otherwise the “benefits” packages should be terminated.

*The PSB should reject Tiered Surcharging proposals as they are:*

- i. Inefficient and encourage Card issuers to avoid full cost recovery from the cardholder beneficiary*
- ii. Expensive and complex for the Merchant for no benefit to the Merchant*
- iii. Fail to send the correct price signals to the cardholder being fundamentally premised on an “age of entitlement”.*

### **5. Correcting the Dis-Information on Service Fees in Taxis.**

As the PSB correctly observes, there has been an orchestrated and ill informed campaign mounted about surcharging. Even the Treasurer was seduced by the dis-information in his comments on releasing the final report of the FSI.

It is necessary to set out the facts with respect to service fees in taxis.

- i. Taxis unlike almost every other good or service offering in Australia is subject to stringent price cap regulation on service fees.
- ii. There are two discrete services provided to a passenger in a taxi by two separate entities. The first involves the point to point at demand transportation service provided by the licensed taxis. The passenger is charged a fare for this service. Secondly a separate specialist payment provider that enables the passenger to pay via an EFTPOS facility offers a separate service. The ATO recognises that there are two discrete services in a taxi.
- iii. Consumers and regulators conveniently ignore the existence of the two services and the separate costs incurred; or the significant public benefits that arise from the provision of EFTPOS services in a taxi reducing reliance on high risk cash transactions and their associated costs.

- iv. The non-cash surcharge collected for providing a payment service in a taxi, independent of the fare, is more than a Merchant Service Fee. The RBA has recognised that there are costs independent of a Merchant Service Fee that need to be recovered including allowing that the payment service provider a return on investment for the capital deployed in providing the service, as is any other business. This is quite a distinct situation not found in most other industries.
- v. None of the regulatory interventions in capping service fees have ever been the subject of any public scrutiny or the application of normal building block models as applies in network industries. Rather they have been capricious and arbitrary activities to impose price caps with no analysis of the public benefits or detriments or the competition impacts of the decisions.

The comments in the FSI report in this regard perpetuate an urban myth that needs to be corrected as a matter of record.

#### **5. Empower the RBA to manage the Card Payment system as the single regulator.**

Multiple regulators enable issues to slip between the cracks and promote regulatory overburden. In recent years we have seen creeping regulation of Card Payments by a range of Commonwealth and State Government regulators, as is the case with Cabcharge card payment products.

The failure of the RBA to intervene and bring Cabcharge's Payment system within the ambit of the other major cards used in taxis has resulted in various State Governments introducing inefficient price cap regulations on taxi non-cash payments service fees resulting in significant competition issues. The "price cap" is a lesson to all those who have argued for such interventions as to why it delivers inefficient and bad market outcomes.

The inaction by the RBA combined with the actions of State regulators has ensured Cabcharge maintained and even increased their market dominance and at the same time continue the practices for which it was fined \$14m (plus \$1.0m costs) in 2010 by the Federal Court for offences under the Competition and Consumer Act. If the RBA had acted on CabFare's application to it in 2012 to "designate" the Cabcharge card and bring it into the regulatory scrutiny of the Payment Systems Board, perhaps this outcome could have been averted.

The RBA needs to be provided with the sole power to regulate all aspects of the Card payment system. This will cut red tape and make the operation of the card payment system more efficient for all participants. For cardholders having multiple points of reference whether it is for consumer protection, EFT Codes of practice, or fee setting is both confusing and time consuming negotiating a regulatory nightmare. If it is not possible to integrate the functions then there needs to be stringer liaison and clear accountability as to which regulator is the lead agency responsible. Having cross membership on Boards (as occurs between APRA and the PSB) or informal annual consultation (as occurs on the critical issues of competition policy between the RBA/PSB and the ACCC) is a recipe for disaster and inaction on critical issues.

Now is the time for the RBA to take decisive action and assume responsibility for all cards used in taxis and limousines. Such action is necessary to remove State Governments and State Taxi and Economic Regulators from meddling in the Banking and Finance system. Something they have demonstrated they are ill equipped to do.

*In summary:* CabFare view is that the PSB should use the opportunity afforded by the FSI's recommendations to examine the entire cost structure of Card Fees and particularly consider moving to a flat Merchant Service Fee. This would:

- i. Make it a simpler and fairer system to all
- ii. Drive down costs to consumers
- iii. Drive down costs to Card Companies.
- iv. Provide Consumers with a simple, easy to understand service fee for using Cards.
- v. Enable the cost of Credit provision to be recovered from the party receiving the credit (i.e. The Cardholder).

This intervention alone would address the key issues flagged by the FSI report.

We are available to meet with the Board to discuss any element of this submission in further detail.

Yours sincerely,



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