



Level 11, 45 Market Street  
Sydney NSW 2000  
**Telephone** 02 9290 7102  
zimmerman@rockportretail.com

## **Submission to the Reserve Bank of Australia**

**Comments on process and content for the Reserve Bank  
review of all card payment types which is due to be held in  
2007/2008**

**12th October 2006**

# Table of Contents

<b>INTRODUCTION AND BACKGROUND.....</b>	<b>3</b>
<b>THE CONDUCT OF THE REVIEW.....</b>	<b>3</b>
<b>THE IMPORTANT ISSUES THAT CONCERN THE AMPF.....</b>	<b>3</b>
Abolition on Interchange Fees for All Card Payments .....	3
The Future of EFTPOS .....	4
Credit Card Interchange Fees .....	4
Transparency of and RBA Control of NEW Scheme Fees .....	4
<b>OTHER MATTERS THAT THE RBA SHOULD INCLUDE.....</b>	<b>5</b>
American Express and Diners Club .....	5
Unbundling of Scheme Debit and Credit Card Fees .....	5
Allowable Costs .....	5
Disputed Transactions and Retrieval Requests .....	5
PIN for Credit Cards .....	5
EMV .....	6
On Us Transactions .....	6
The EFTPOS System .....	6
Other Payment Systems .....	6
Fraud reporting .....	7
Costs of Payment Systems .....	7

## **Introduction and Background**

The Reserve Bank of Australia (RBA) has requested interested stakeholders to make written submissions relating to the content and process of the 2007 – 2008 payments review.

The AMPF met recently to discuss content it considers relevant to the review and how they would like to see the review conducted.

The AMPF has in the past, engaged with the Reserve Bank and other stakeholders to present the views of its members which represent a broad cross-section of merchants ranging from the smallest operator to the largest multi-national organisations. Membership of the AMPF includes some 12,000 members of the Australian Retailers Association (ARA), BP, Caltex, Mobil, Mitre 10, Bunnings, Coles, Woolworths and Australia Post

## **The Conduct of the Review**

The AMPF would like the RBA to identify and publish details of all stakeholders it will consult with during the process of the review.

The AMPF would ask the RBA to clearly articulate:

- its vision for the future of all payment systems.
- what is the time-frame to complete and implement the review of payments systems

It is essential that merchants and other players in the payments systems understand what the future holds in order to plan for change and develop business cases so they may invest in the required infrastructure.

Research and consideration to leading practice from around the world in order to evaluate what lessons or alternative models might apply in Australia, particularly around the architecture and governance of the payments system and business models.

In the past the AMPF has made presentations to the RBA in addition to the public consultation process. We believe this engagement has proven to give the best outcome and would encourage the RBA to continue to consult the AMPF, as well as conducting regular meetings with all stakeholders.

The AMPF recommends the setting up of an advisory group of stakeholders and industry experts to assist the RBA in its deliberations. Not only will this group provide input and advice to the RBA, it may well assist in achieving outcomes via a consultative process which we understand is the RBA's preferred approach.

The AMPF would like to seek clarification of the role the ACCC should play (if any) in the Review process.

In summary, the AMPF believes that the RBA should clearly define the objectives, timeframes, process and scope of the review and that the RBA make a suitable announcement of its intentions once the review process has been agreed.

## **The Important Issues that Concern the AMPF**

### **Abolition of Interchange Fees For All Card Payments**

The AMPF has stated on the record that the abolition of (or ZERO) interchange should be considered by the RBA. This notion was flagged by Phillip Lowe in his final presentation to the Standing Committee on Economics Finance and Public Administration held in Sydney in mid 2006 as an interesting idea worth considering.

## **The Future of EFTPOS**

As noted in the communication to you of the 30<sup>th</sup> September 2006 the AMPF is concerned that both Visa and MasterCard are determined to promote the use of "Scheme Debit Cards" at the expense of the more efficient, lower resource cost, shorter transaction time and lower processing cost domestic bi-lateral EFTPOS system. The AMPF believes that EFTPOS is Australia's most efficient payment system and wishes to ensure that its future remains secure and continues to provide optimal service at the least cost to both merchants and cardholders.

The AMPF would consider it a tragedy if EFTPOS was allowed to disappear and was displaced by higher cost, less secure options such as those offered by the international card schemes.

In order to ensure the future of EFTPOS urgent attention is required to develop international acceptance capability and to develop card not present capability.

## **Credit Card Interchange Fees**

In the event that zero interchange is not introduced, the current range of eligible cost components should be reviewed. Credit card interchange fees contain a number of components which are classified as eligible costs - these include fraud and fraud prevention costs and the cost of providing an interest free period. The AMPF believes that these costs should be removed as allowable cost categories and allow these payment tools to compete on their merits rather than having merchants subsidise these costs for the card issuing institutions.

In any case, for reasons of transparency, the percentage of the total interchange fee that each cost category comprises should be published. As this is consolidated across all issuers and all credit card schemes, there is no issue of this being "commercial-in confidence" data.

The AMPF has consistently argued that interchange fees are to be determined on a cost basis, then all costs must be considered. There seems to be no logical arguments why only issuer costs (as is the case for credit and scheme debit cards) or only acquirer's costs (as is the case for EFTPOS) should be included.

## **Transparency of and RBA Control of NEW Scheme Fees**

Since the RBA designated credit card interchange fees, new scheme fees have been developed and introduced as a "back-door" means of clawing back lost revenue streams.

Despite the RBA's best efforts to regulate the payments systems it could be argued that interested parties are actively developing new means of by-passing regulations typically at the merchants' expense.

The AMPF calls for transparency in all facets of the construction of merchant service fees levied by the banks and card schemes on the merchant community and for the RBA to take leadership as to what is or is not included in allowable costs.

The merchants have had these costs passed on but it is not clear exactly what the value proposition is for these fees and what the merchant is getting for their dollar spend. The merchant should have the choice of paying the scheme fees and receiving the benefit or not paying the scheme fees and not receiving the benefit. At this point in time it is not clear what the benefit to the merchant is for the scheme fees.

Any review of interchange fees should be broadened to include all fees levied by the card schemes to avoid back door methods of transferring funds from acquirers to issuers.

## **Other Matters that the RBA should Include**

### **American Express and Diners Club**

Since reduced credit card interchange fees were introduced in late 2003, card issuers have looked for ways to maintain their income resulting in a proliferation of co-branded cards launched into the market place. Co-branded card arrangements brokered with Diners Club and in particular American Express has resulted in increased merchant service fees.

Merchants (in particular those without market power) are concerned that they are now between a rock and a hard place.

Should they refuse to accept high cost payment methods they will lose business to their competitors – should they choose to surcharge they may still lose the customer to the competitor. The course of action most readily available to merchants is to build in these costs into the pricing of their merchandise thus hiding (and therefore defeating) the RBA's reasons for reducing interchange fees. As a result most consumers may then pay a higher price irrespective of whether or not they pay using a high cost payment card.

### **Unbundling of Scheme Debit and Credit Card Fees**

Following the RBA's designation of both EFTPOS and Scheme Debit interchange fees small merchants have advised the AMPF that all merchant service fees will be bundled.

Merchants believe that acquirers must develop the capacity to separate these fees to ensure transparency. The AMPF would like the RBA to consider appropriate regulation to ensure ongoing transparency.

### **Allowable Costs**

The AMPF would like the RBA to clearly enunciate both the methodology and the allowable costs which are used to calculate interchange fees.

For example, merchants may be required to upgrade their POS terminals to cater for chip or PIN at POS both of which are designed to reduce fraud. However until the RBA completes its review the cost of fraud remains an allowable cost which the merchant will continue to pay through interchange. So merchants are paying for fraud and fraud prevention through interchange and also paying to upgrade to reduce fraud. Is this double dipping?

### **Disputed Transactions and Retrieval Requests**

The cost of investigating disputed transactions is extremely costly for issuers, acquirers and merchants.

On many occasions a merchant is required to validate a transaction only to find that it was authentic. The bank is able to charge a fee to the cardholder who (wrongly) questions the charge if it was correct however the merchant who does the work is not compensated for time and effort.

### **PIN for Credit Cards**

PIN on Credit card would reduce the number of disputed transactions and as a result reduce the administration cost to issuers, acquirers and merchants. Based on the number of disputes for PIN based debit card transactions to signature based credit card transactions the introduction of PIN validation on all credit card transactions would result in a 70-80% reduction in the number of disputes.

The AMPF has been on record requesting that PIN on Credit card be introduced as a matter of urgency. The timetable for introduction is now February 2008. The AMPF wants assurance that this time table will not be further prolonged.

The AMPF also notes that when PIN at POS on credit is introduced in early 2008, it will be up to the issuer to determine if they will offer this service to their cardholders. Mandatory PIN on credit card transactions must be the goal.

## **EMV**

The introduction of EMV has also been discussed many times over the past 10 years– a time table for the introduction of Chip and PIN should be set by the RBA and strictly adhered to.

## **On Us Transactions**

The AMPF would also like the RBA to review the charging of interchange, scheme fees as well as processing fees at the same levels for “on us” transactions as they do for “off us”. This is despite the efficiencies that are realised but not passed on to the retailer.

## **The EFTPOS System**

In Australia, unlike in other countries such as Canada, there is no such thing as an EFTPOS brand owner and as such the development and enhancement of EFTPOS has not been vigorously pursued.

If EFTPOS is to survive it needs ownership to be taken by the participants to determine future functionality and to drive development of the EFTPOS system. This raises a number of issues, for example:

- ✚ What should be APCA’s involvement and responsibility?
- ✚ Is there any potential for a central switch as in some models?
- ✚ How and who is going to take responsibility to attract new entrants into the EFTPOS system?

Visa and MasterCard are actively marketing the benefits of Scheme debit cards at the expense of EFTPOS. Do the banks want to disband EFTPOS as they did with Bankcard? Will EFTPOS fold due to lack of investment by the owners of the EFTPOS system?

What is the RBA view of EFTPOS and does it see EFTPOS being a credible third payment system in the future? If EFTPOS is allowed to fold, then merchants and ultimately the public will pay higher fees for scheme debit card transactions. Can the RBA drive innovation so that for example secure payments may be made with an EFTPOS card for internet transactions?

## **Other Payment Systems**

The AMPF would like to see the RBA broaden the review to take into account the other payments systems such as:

- B.Pay
- ATM’s
- Open Loop Pre Paid Schemes
- Non Scheme Cards i.e. American Express, Diners and JCB

This review should consider the effects interchange or payments between participants such as (but not limited to) payment from American Express and Diners Club to partner banks have on the overall payment landscape especially where the payment tools are substitutable.

The RBA should take a holistic approach and ensure the same philosophies and principles are applied to all payment systems (eg issuer’s costs for credit vs acquirer’s costs for EFTPOS)

The AMPF with the help of the Australian Retailers Association in association with the RBA would like to re conduct the survey of smaller merchants to obtain their views on costs of merchant fees after the current reforms that have occurred since the last survey in 2001.

### **Fraud Reporting**

The AMPF has previously requested that comprehensive and regular fraud reporting be publicly available to allow informed debate on this vital issue.

### **Costs of Payment Systems**

It would be helpful if there was accurate data publicly available on the cost of various payments systems. This would aid in the evaluation and debate on various payment systems issues. The AMPF and ARA would be happy to assist in the collection of merchant data for such a study.