

Merchant Card Payment Costs and Surcharging - October 2024

2024

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Executive Summary

The Reserve Bank of Australia (RBA) is conducting a review of merchants' card payment costs and surcharging. Australians use cards extensively to pay for goods and services and benefit from the convenience and security provided by card payments. However, in an environment of heightened concern around the cost of living and ongoing changes in payment preferences, merchants and consumers are increasingly focused on card payment costs and surcharging. These two issues are linked as merchants would be less likely to surcharge consumers if card payment costs were lower. Accordingly, it is timely to review whether the RBA could do more to put downward pressure on merchant card payment costs by promoting competition and efficiency and whether the RBA's surcharging framework remains fit for purpose. This review also recognises that some years have now passed since the surcharging framework was introduced.

This issues paper provides a high-level overview of the RBA's review and invites stakeholders to provide feedback on the RBA's existing regulations and potential regulatory responses. Section 1 describes the background and process for this review. Section 2 highlights recent issues relating to card payments and discusses some potential regulatory responses that the RBA could consider, including whether:

- the RBA's existing regulations and initiatives on interchange and scheme fees, least-cost routing (LCR) and surcharging continue to achieve their desired outcomes
- greater transparency in fees should be required from payment service providers (PSPs) and card schemes to promote competition and efficiency and put downward pressure on merchant card payment costs
- issues beyond the scope of this review have implications for the design of policies for card payments and vice versa.

Interested stakeholders are invited to provide written submissions by 3 December 2024. Section 3 provides details on how to make a submission.

Detailed assessments of stakeholder submissions and reform proposals will form the next stage of this review. If the Payments System Board forms a view that consultation on regulatory action is in the public interest, the RBA will further consult on any reform proposals prior to any decisions being made.

1. Background

The RBA has regulatory powers in respect of payment systems and their participants under the *Payment Systems (Regulation) Act 1998* (PSRA). Under the *Reserve Bank Act 1959*, the RBA's payments system policy is set by the Payments System Board (PSB) and aims to control risk in the financial system, promote the efficiency of the payments system and promote competition in the market for payment services consistent with the overall stability of the financial system. The RBA has used these powers since the early 2000s to introduce standards and access regimes relating to card payments and has periodically reviewed its regulations to ensure they remain fit for purpose given ongoing changes in the payments landscape.

The RBA is conducting a Review of Retail Payments Regulation (Review), with the first phase of the Review focusing on merchant card payment costs and surcharging – the subject of this issues paper. A series of 'Backgrounders' providing general information on relevant payments topics discussed in this paper is available separately, as referenced throughout this paper.

The RBA recognises that there are other payments issues that have implications for the safety, efficiency and competitiveness of the payments system. Subsequent phases of the Review will focus on a range of issues in the broader payments ecosystem, including issues that would be better addressed after the passage of proposed amendments to the PSRA that are currently before the Australian Parliament (see Section 3.1 for further details).

Stakeholders are invited to provide written submissions on issues that they think the RBA should consider in this phase of the Review relating to merchant card payment costs and surcharging. Key questions for stakeholders are included in Section 2 and collated in Appendix A. The RBA will review written submissions received and endeavour to meet with key stakeholders to discuss their submissions in more detail. If in the PSB's view there is a public interest case for consulting on regulatory action, the RBA will prepare and release detailed regulatory proposals for further consultation.

For a list of current RBA interventions, see the Backgrounder on the RBA's Current Payments Regulations.

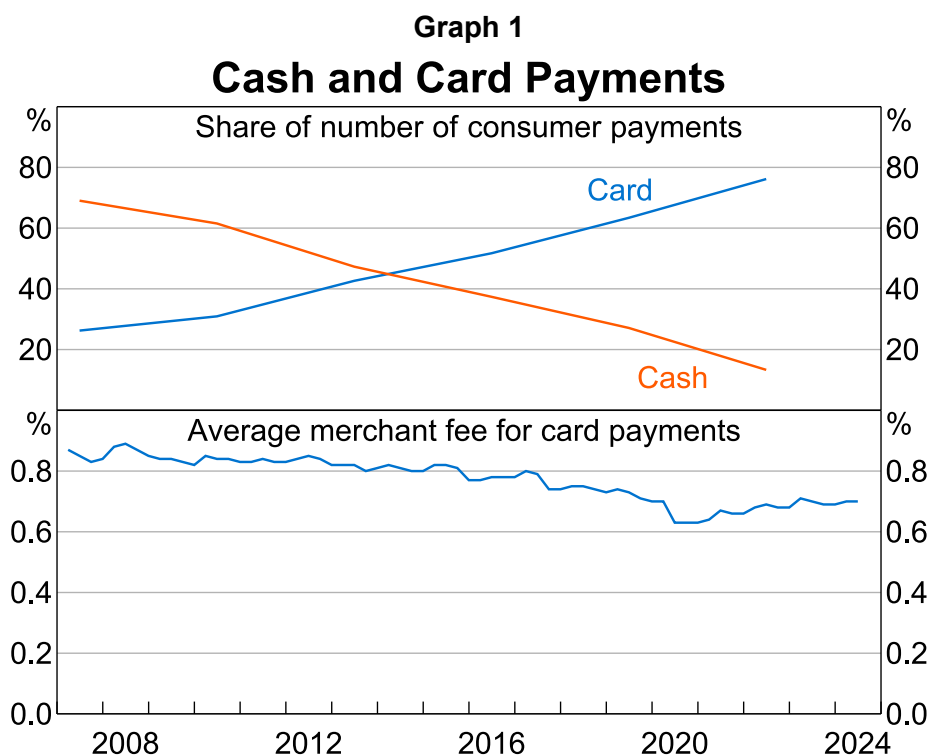
2. Issues for Consultation

2.1. Overview

This phase of the Review is focused on merchant card payment costs and surcharging. In an environment of heightened concern around the cost of living and ongoing changes in payment preferences, merchants and consumers are focusing more on these issues. Merchant costs and surcharging are interrelated issues: merchants would be less likely to surcharge consumers if card payment costs were lower. Accordingly, it is timely to review whether there are further regulatory actions the RBA could take to put downward pressure on merchant card payment costs by promoting competition and efficiency, and whether the RBA's surcharging framework remains fit for purpose. This review also recognises that some years have passed since the surcharging framework came into effect.

Merchant card payment costs

Cards (including debit, prepaid, credit and charge cards) are the most frequently used payment method in Australia, accounting for three-quarters of all consumer payments in 2022 (Graph 1). This follows a long-run shift by consumers away from paying with cash to using cards. When a merchant accepts a card payment, they are typically charged a 'merchant service fee' by their PSP for processing the transaction.¹



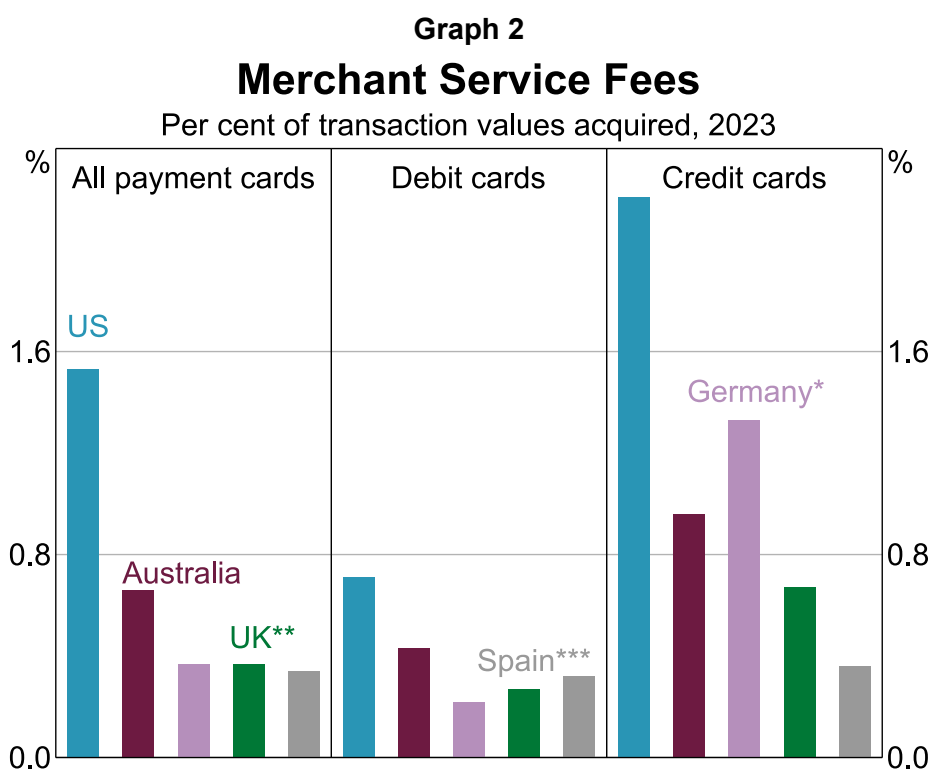
Sources: RBA; RBA calculations, based on data from Colmar Brunton, Ipsos and Roy Morgan Research.

Given the prominence of card payments in Australia, the RBA views merchant card payment costs as a key indicator of efficiency and competition in the payments ecosystem. The RBA has introduced reforms since the early 2000s that have put downward pressure on merchant card payment costs (Gill, Holland and Wiley 2022).

The average fee that merchants pay for each card payment has declined over the past two decades (Graph 1). However, increased use of cards by consumers has led to overall card payment costs for merchants rising to an estimated \$6.4 billion in 2022/23. This has at least partly been offset by declines in other payment costs, such as those associated with accepting cash payments.

There are several areas where the efficiency and competitiveness of card payments could be improved:

- **Merchant service fees in Australia are higher than in some other economies, including some that also regulate interchange fees.** While the average card payment fee in Australia is lower than in some advanced economies such as the United States, it is higher than in some other jurisdictions such as Europe (Graph 2). This suggests that there may be room for further reductions in card payment costs, particularly as the fixed costs of providing card payment services are being spread over a higher volume and value of transactions than ever before.



* 2017 data.

** 2022 data.

*** Excludes three-party schemes.

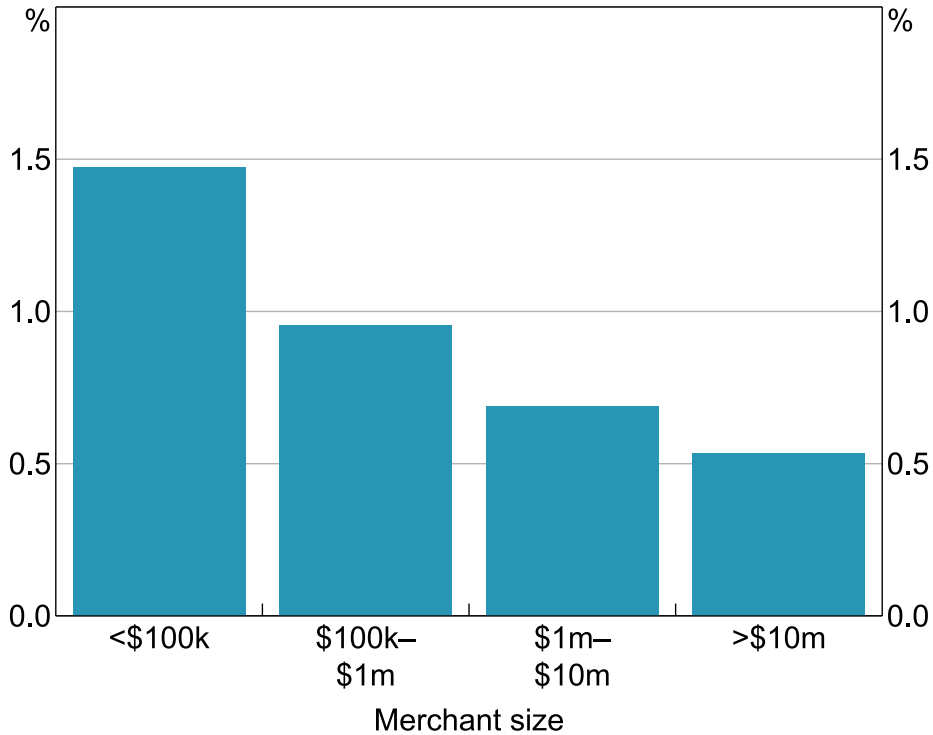
Sources: Banco de España; British Retail Consortium; Deutsche Bundesbank; Nilson Report; RBA.

- **There is a big difference between the fees paid by large and small merchants in Australia.** The average per-transaction fee (‘cost of acceptance’ for card payments) paid by small merchants is around *three* times that paid by large merchants (Graph 3).

Graph 3

Merchant Service Fees by Merchant Size*

Per cent of value of card transactions, 2022/23



* Weighted average. Merchant size based on annual value of eftpos, Mastercard and Visa transactions. Merchant Service Fees exclude GST.

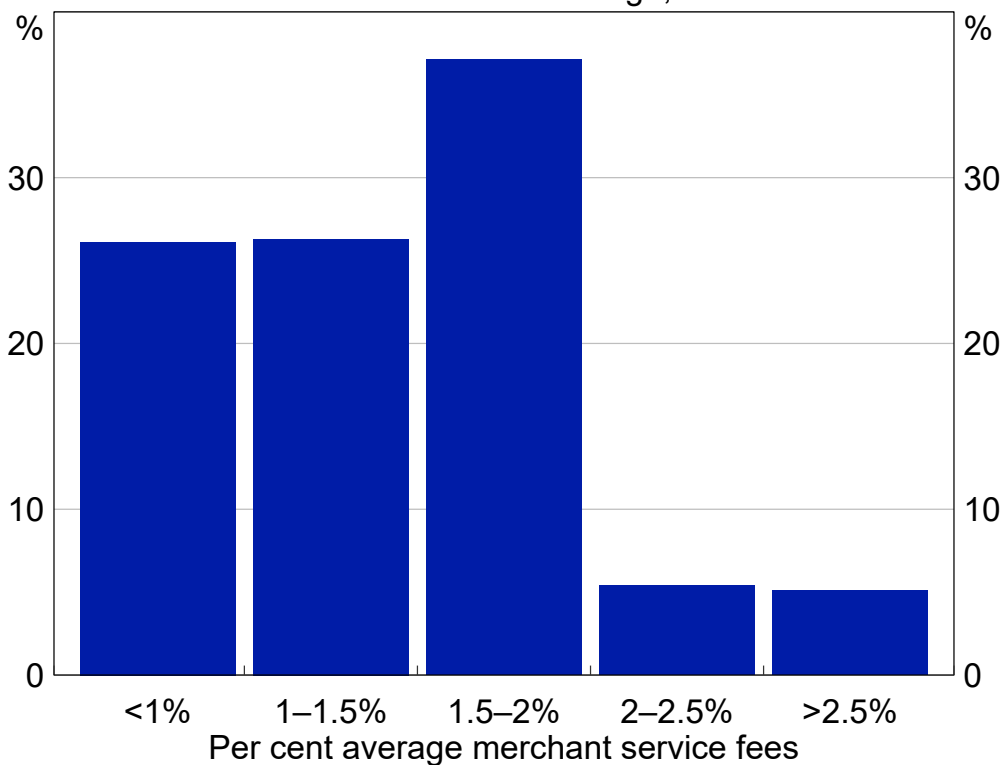
Source: RBA.

A key driver of this difference is the ability of larger merchants to negotiate favourable wholesale fees for processing card transactions – particularly through ‘strategic’ interchange rates – and a lower margin from PSPs. The fees paid by small merchants also vary widely, with costs of accepting card payments ranging between less than 1 per cent to well over 2 per cent of transaction value (Graph 4).

Graph 4

Small Merchants – Merchant Service Fees*

Share of small merchants with
merchant service fees in range, 2022/23



* Weighted average. For merchants with less than \$1m transactions in 2022/23. Merchant size based on annual value of eftpos, Mastercard and Visa transactions. Merchant Service Fees exclusive of GST.

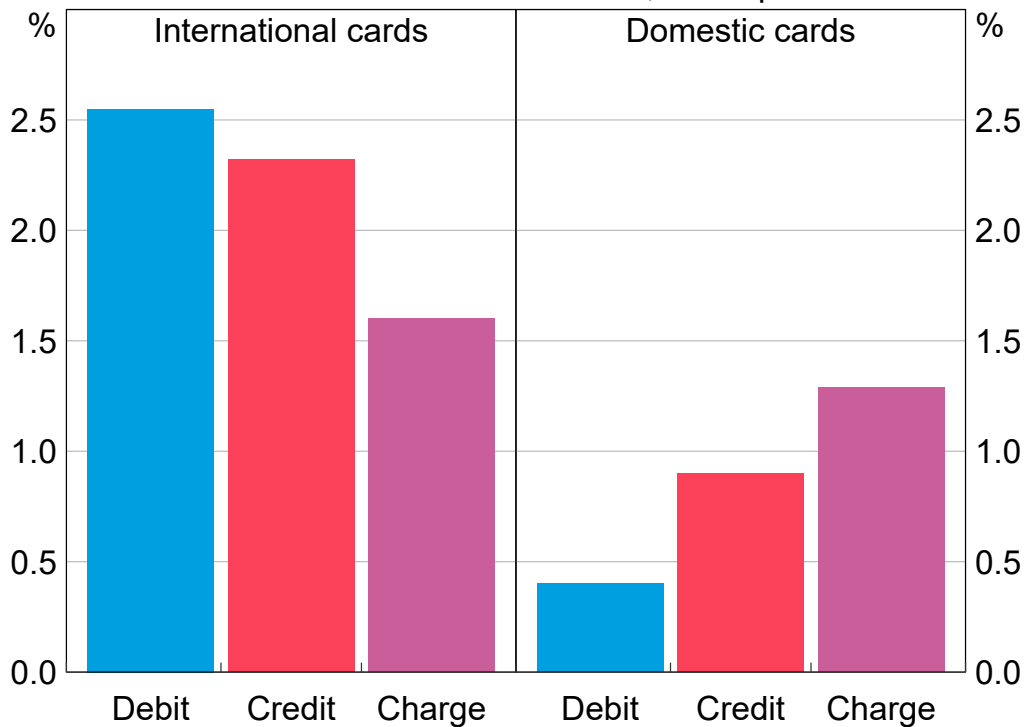
Source: RBA.

- **Transactions on foreign-issued cards are particularly expensive for Australian merchants to accept.** On average, these transactions cost Australian merchants around 2½ per cent for debit and credit cards, which is several times larger than the cost of equivalent transactions on domestic cards (Graph 5). The high cost of foreign card transactions for Australian merchants appears to be mainly due to high wholesale costs: interchange fees can be as high as 2.4 per cent and net scheme fees are around 1.6 per cent.

Graph 5

Merchant Service Fees

Per cent of value of card transactions, June quarter 2024



Source: RBA.

- **The cost of card payments is often opaque and difficult to understand.** There is limited publicly available information on PSPs' retail prices, wholesale costs, margins and transaction volumes. This can make it hard for merchants to compare pricing and switch between PSPs for a better deal. Interchange fee schedules from card networks have grown in complexity over time and their scheme fee schedules are even more complex and not publicly available. The limited information on wholesale costs may reduce the competitive pressure on card networks to lower their fees. It can also make it hard for merchants to understand the fees that they are paying and identify ways to reduce their costs.

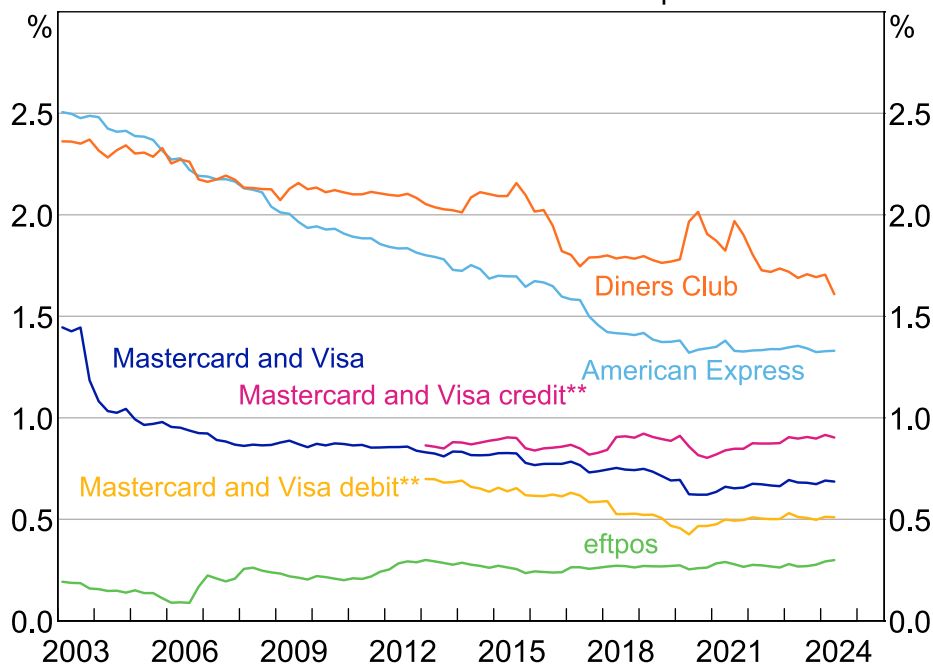
For more information on interchange and scheme fees, see the Backgrounder on Interchange and Scheme Fees.

Surcharging

The RBA's surcharging regulations allow merchants to surcharge consumers for the reasonable cost of accepting card payments. The RBA's regulations were introduced in 2003 following the 1996–1997 Financial System Inquiry and joint research on card payments by the RBA and the Australian Competition and Consumer Commission (ACCC). The RBA's regulations aim to promote the efficiency of the payments system by encouraging consumers to use lower cost payment methods and put competitive pressure on card networks to lower their wholesale fees. The ACCC has powers to take action against merchant surcharging that exceeds the merchant's cost of card acceptance. Some benefits of surcharging are:

- **Surcharging allows merchants to directly recover their card payment costs.**
- **Surcharging can be used by merchants to signal to consumers that they are using a relatively expensive payment method** and may encourage them to switch to using lower cost payment methods. Surcharging is likely to have contributed to the pronounced shift by consumers away from (higher cost) credit cards towards (lower cost) debit cards over the past two decades.
- **The ability to surcharge places pressure on PSPs and card networks to lower the fees they charge**, as surcharges can incentivise consumers to switch away from using payment methods with high costs. The RBA's view is that preventing card schemes from imposing 'no-surcharge' rules and allowing surcharging at the reasonable cost of acceptance have made a significant contribution to the long-run decline in the average fee that merchants pay for card transactions. The decline in fees for three-party schemes – American Express and Diners Club – is particularly notable, given that these networks are not subject to the RBA's interchange regulation (Graph 6).

Graph 6
Total Merchant Fees*
Per cent of transaction values acquired



* Series break in September 2020 due to change in reporting forms and in December 2022 due to change in collection coverage.
 ** Prior to changes in reporting methodology in June 2018, the average fee reported for Visa and Mastercard debit cards was slightly overstated and the average fee reported for Visa and Mastercard credit cards was slightly understated; the overall average fee for Visa and Mastercard was unaffected by the reporting change.

Source: RBA.

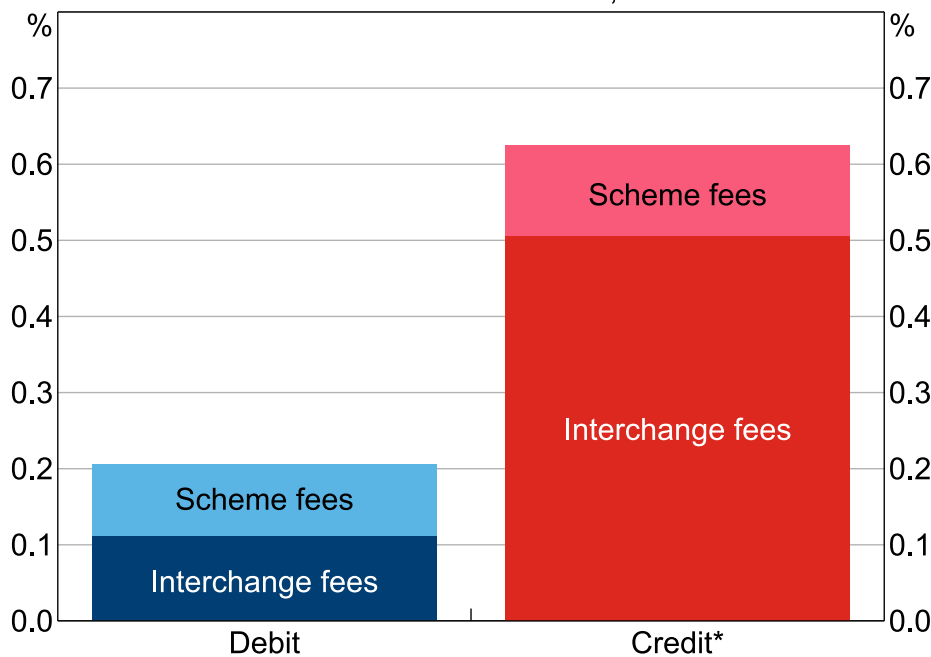
However, some changes in the payments landscape since the surcharging rules were introduced may be reducing their effectiveness. In particular, consumers' use of cash has declined significantly. In the mid-2000s, cash was the most commonly used retail payment method and was typically not surcharged, despite merchants also incurring costs to securely store and handle cash. By 2022, cash was used for just 13 per cent of transactions, with debit cards used for over half of all retail payments (Nguyen and Watson 2023). Growth of online shopping has also increased the share of transactions where cash cannot be used. At the same time, more merchants are

choosing to surcharge card payments. According to the RBA's Consumer Payments Survey, in late 2022, 7 per cent of card transactions were surcharged, up from 5 per cent in 2019 (Livermore *et al* 2023); anecdotal evidence suggests that the share of card transactions being surcharged has risen further since then. The incidence of surcharging is higher in some sectors, such as cafes, restaurants and pubs, than in others, such as supermarkets. The approach of PSPs to pricing card payments has also changed in recent years. Some PSPs are offering 'automatic' surcharging capabilities to merchants, and so marketing their payment services as 'free' for merchants. Merchants, especially smaller businesses, are also increasingly taking up single-rate plans that charge the same percentage fee for all card transactions.

These trends have contributed to growing public concern about payment surcharges. Issues raised with the RBA include:

- **Consumers are less able to avoid surcharges**, because fewer consumers use or carry cash. The growth of online shopping has also increased the share of transactions where cash cannot be used.
- **Consumers dislike surcharges**, which is consistent with findings of the behavioural economics literature that people view surcharges as a loss and equivalent discounts as a gain. Since people are loss averse, they dislike the perceived loss from a surcharge (Kahneman and Tversky 2000).
- **Consumers sometimes do not know whether a surcharge will be applied, or how much it will be**. This may be because some merchants do not disclose their surcharge rates as they are required to. The rise of contactless payments also makes it difficult in many circumstances for the actual dollar amount of any surcharge to be displayed to the consumer before the payment is finalised, as it can depend on what type of card is 'tapped' at the terminal.
- **Some merchants may be charging excessive surcharges**. Surcharges are considered excessive if they are greater than the merchant's cost of accepting the card payment.
- **Debit, credit and charge card transactions are often surcharged at the same rate**, due to the rise of single-rate payment plans, which can be attractive to merchants for their simplicity. Such single rates are not reflective of the cost of processing debit, credit and charge card transactions. This means that consumers may be paying more than necessary for debit card transactions, given debit card transactions are much cheaper to process than credit card transactions (Graph 7). It also means that the price signal for consumers to use a lower cost payment method like debit – a key objective of the surcharging framework – is dampened. In other words, consumers using higher cost payments methods (such as credit cards) are being cross-subsidised by those using lower cost methods (such as debit cards).
- **PSPs are increasingly bundling a range of services with their card acceptance services**, leading to a higher fee that can then be passed on to consumers as a payment surcharge. Some single-rate payment plans also bundle in services unrelated to card payments, such as business data or inventory management services, the cost of which is then passed on to consumers through a payment surcharge.

Graph 7
Wholesale Costs of Card Payments
 Per cent of transaction values, 2023/24



* Calculated by taking each scheme's weighted average credit interchange rate and weighting those rates by the number of transactions for each scheme.

Source: RBA.

Some of these concerns, particularly around lack of disclosure and excessive surcharging, reflect the difficulty of ensuring compliance with the surcharging rules. The large number and small size of many merchants makes enforcement challenging for the relevant competition authorities. It is difficult for consumers to hold merchants to account because they have no way of knowing the card payment costs of individual merchants, which can vary significantly. There is also a distinct lack of data available to policymakers and the public on surcharging practices.

For more information on surcharging, see the Backgrounder on Payment Surcharges in Australia.

2.2. Interchange fees

Interchange fees are paid by the merchant's PSP to the customer's card issuer when a card payment is made, with the PSP passing on these costs to the merchant. These wholesale fees are typically set by the card network, and they can make up a sizeable share of the card payment fees paid by merchants. The RBA has set caps and weighted-average benchmarks for interchange fees, which have helped to reduce card payment costs and limit the dispersion of fees paid by merchants of different sizes. The RBA's view is that interchange regulation has contributed to a more efficient payments system. However, interchange fee schedules have grown in complexity and the cost of card payments remains substantial for small businesses, which pay much higher interchange fees than large businesses. In this context, the RBA seeks stakeholder views on whether changes should be made to the current interchange rules.

The level of interchange fees

The level of interchange benchmarks and caps was last considered in the 2019–2021 Review of Retail Payments Regulation, following recommendations by the Black Economy Taskforce (2017) and the Productivity Commission (2018) that interchange fees should be reduced or even eliminated. These recommendations were based on the argument that there is little justification for such fees in mature card systems, such as in Australia. At that time, the PSB decided not to lower the weighted-average interchange benchmarks, noting that interchange fees in Australia were relatively low by international standards and the existing framework had contributed to more efficient outcomes, including a significant shift to debit cards from credit card payments. However, the PSB did not rule out lowering these benchmarks in the future.²

The RBA is interested in stakeholders' views on whether there is now a policy case for lowering the interchange benchmarks. Lower interchange fees should feed through to lower card payment costs for merchants and could reduce the incentive for businesses to surcharge card payments. For credit transactions, the weighted-average interchange benchmark (0.5 per cent) and cap on individual fees (0.8 per cent) in Australia are higher than in some other jurisdictions, notably Europe (which has a cap of 0.3 per cent). The weighted-average cap in Australia of 0.5 per cent, which is based on calculations of eligible scheme costs for issuers from 2006, is likely to be out of date, particularly as the fixed costs of providing card issuing services are now spread over a much larger volume of transactions (RBA 2006). It is also debatable whether some of the costs included in that calculation, particularly funding costs related to interest-free periods, should be borne by merchants. Other jurisdictions are also examining how interchange benchmarks and caps should be set, with the New Zealand Commerce Commission recently questioning whether there should be any difference between interchange fee caps for credit and debit transactions (Commerce Commission 2024).

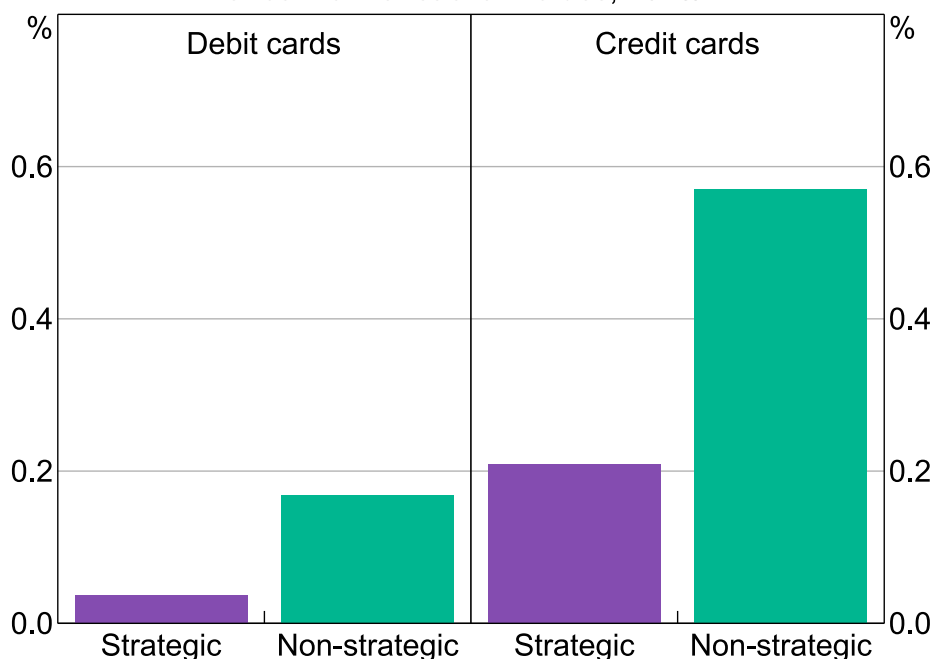
For debit card transactions, the weighted-average interchange benchmark (8 cents) and cap on individual interchange fees (10 cents or 0.2 per cent) is at a broadly similar level to interchange regulations in some other jurisdictions such as the United Kingdom and Europe (caps of 0.2 per cent). The average value of debit card transactions has remained relatively stable since the 2019–2021 Review, so the cents-based benchmark and cap would not have risen as a percent of the average value. However, there has been strong growth in the number and value of debit card transactions over the past five years, which should have put downward pressure on the cost per debit card transaction for issuers.³ Furthermore, the weighted-average interchange rate on debit cards has drifted noticeably below the benchmark over recent years in response to competition between the card networks. This suggests that the benchmark may now be too high.

As noted above, the cost of card payments remains substantial for small businesses. This is partly because large merchants have the bargaining power to directly negotiate much lower 'strategic' interchange rates from the card networks (Graph 8). The RBA is not aware of evidence to suggest that issuers face different card processing costs for smaller merchants compared with larger merchants. So the large gap between the interchange rates for small merchants and large merchants is difficult to justify.

The RBA seeks feedback on whether there is a case for regulatory intervention to narrow the gap between strategic merchant rates and the rates paid by small businesses. Possible interventions include imposing a floor on interchange rates, a maximum range between the highest and lowest interchange rates by network or reducing interchange caps for small business transactions, as has occurred in Canada for small businesses following an agreement between the Canadian Government and Visa and Mastercard (Government of Canada 2023).

Graph 8 Domestic Interchange Fees by Merchant Type*

Per cent of transaction values; 2023/24



* Strategic interchange fees are available for typically larger merchants who meet certain requirements (e.g. volume requirements) as defined by the schemes.

Source: RBA.

Foreign card transactions

The cost of foreign card transactions is much higher for acquirers and merchants in Australia than for equivalent domestic card transactions. When a foreign card is presented at an Australian merchant, an interchange fee is paid by the merchant's acquirer to the foreign issuer of the card. Previous RBA reviews have decided against applying interchange caps to foreign card transactions because the share of card payments made by foreign-issued cards was low and there was no evidence of issuers attempting to circumvent the Australian interchange regime by issuing cards offshore. However, since 2022, the RBA has required card networks to publish their interchange fee schedules for foreign card transactions on their websites. These schedules show that interchange rates on foreign card transactions can be as high as 2.4 per cent, which is three times the highest domestic credit interchange rates. As a result, foreign cards used in Australia are estimated to account for around 8 per cent of total interchange fees paid by merchants in Australia, despite only accounting for around 3 per cent of total transactions.⁴ These high costs for foreign card transactions may also be raising costs for domestic card transactions given the rising prevalence of single-rate plans and therefore contributing to higher surcharges.

The RBA seeks feedback on whether there is a case for capping the interchange fees on foreign card transactions in Australia, as occurs in Europe. For in-person transactions, European inter-regional interchange fees are capped at 0.2 per cent for debit cards and 0.3 per cent for credit cards; for online transactions the caps are set at 1.15 per cent for debit cards and 1.5 per cent for credit cards. The UK Payment System Regulator is proposing an interim cap of 0.2 per cent for UK-European Economic Area (EEA) consumer debit transactions and 0.3 per cent for consumer credit transactions where the transactions are made online at UK businesses (Payments System Regulator 2023). The New Zealand Commerce Commission is also considering interchange caps for foreign card transactions in New Zealand (Commerce Commission 2024).

Interchange complexity and transparency

Interchange fee schedules have become more complex over time. The increase in the number of interchange categories has been associated with developments including:

- the introduction of new infrastructure, such as tokenisation
- the introduction of new products, such as instalments programs
- responses to competition, such as special rates for small and medium businesses
- the splitting of categories into card present and card not present.⁵

While varying interchange fees could be useful for incentivising certain behaviour from acquirers and merchants, such as encouraging tokenised transactions online, the case for differentiation is not always clear. For example, it is not obvious why interchange rates should be higher for in-person transactions when using a mobile wallet rather than a physical card or why interchange rates need to be higher for online transactions.⁶ Interchange fee complexity makes it hard for merchants on unblended plans to understand and check their costs, and compare service fees across PSPs, which may hamper competition.⁷

The RBA seeks feedback on whether there is a case to reduce the complexity, and/or enhance the transparency, of interchange fees. In particular:

- Should the card networks be required to publish aggregate data on the average interchange fees on transactions to promote transparency and competition? This would be in addition to the existing requirement in the RBA's regulations that designated card networks publish their interchange fee schedules.
- Should there be a limit on the number of different interchange categories that a card network can set?
- Should the interchange caps be only cents-based? The argument for a cents-based cap, rather than ad valorem, for debit transactions is that most costs of processing are unrelated to the transaction value. For example, the messaging cost for a \$1 payment is arguably no different to that of a \$100 payment. Also, debit transactions are not subject to many of the ad valorem costs associated with credit cards, such as interest-free periods and rewards. This argument could also be extended to credit transactions if costs such as interest-free periods and rewards should not be borne by the merchant through interchange fees.
- Should the RBA's interchange regulation be simplified by just having caps, rather than both caps and benchmarks? If so, would the interchange caps need to be lowered to prevent an increase in average interchange fees? Following the 2015–2016 Review of Card Payments Regulation, the RBA supplemented the weighted-average benchmarks with caps on individual interchange fees; this was to narrow the range of interchange fees and limit the fees that could be charged to small businesses. A key argument for the weighted-average benchmark is that it limits the average level of interchange while providing the card networks with flexibility in setting their interchange schedules, including to offer premium products that compete with three-party schemes. However, the RBA is not aware of any other jurisdiction that uses both weighted-average benchmarks and caps, which suggests that it may not be necessary to retain both for interchange regulation to be effective. The removal of the benchmarks could reduce the regulatory and administrative burden on the payments industry from the constant resetting of interchange fees by the schemes to maximise the average interchange.⁸

Net compensation

The 'net compensation' provisions in the RBA's regulations, which are designed to prevent circumvention of the interchange fee caps and benchmarks, appear to be operating broadly as intended. However, the RBA has become aware of a potential regulatory gap where indirect issuer participants sponsored by *overseas* entities may not technically be captured, either directly or indirectly, by the net compensation provisions. The RBA is not

aware of this potential regulatory gap being exploited. However, to ensure a level playing field, the RBA proposes to consult on proposed amendments to the net compensation requirements designed to ensure that *all* Australian issuers are subject to them, irrespective of the domicile of any sponsor.

The RBA also welcomes comments on any other aspects of the interchange regulations.

For more information on interchange and scheme fees, see the Backgrounder on Interchange and Scheme Fees.

Q1: Is there a case for lowering the level of interchange benchmarks or caps? Should the difference between the interchange fees paid by big and small businesses be limited in some way?

Q2: Should interchange regulation be extended to foreign card transactions in Australia?

Q3: Is there a case for reducing the complexity, and/or enhancing the transparency, of interchange fees? If so, how?

2.3. Scheme fees

Card acquirers and issuers pay scheme fees to card networks such as Visa, Mastercard and eftpos for using their services. These wholesale fees make up a significant share of overall card payment costs. In 2023/24, Australian acquirers paid around \$1.4 billion of scheme fees (net of rebates) and issuers paid \$0.4 billion. These fees are ultimately passed on to merchants and consumers, with the scheme fees charged to acquirers accounting for around one-fifth of the total card payment costs for Australian merchants.

Scheme fees have risen over time, putting upward pressure on card payment costs for merchants. There is also considerable variation in scheme fees between different card networks. It is unclear to what extent these observations reflect differences in the cost and quality of services provided by the networks. Unlike interchange fees, there are no regulations restricting the level of scheme fees. The rise in scheme fees may reflect a lack of competition in the card payments market.

The main sources of competitive pressure on scheme fees for acquirers in the debit market are:

- surcharging
- dual network debit cards allowing transactions to be routed through two different networks
- the adoption by merchants of LCR functionality, where transactions can be routed to the least-cost debit card network.

Consistent with this, in recent years, debit scheme fees were consistently lower for transactions that were routable to eftpos (in-person transactions made with a physical card) than for transactions that were not yet routable (mobile wallet and online transactions) (Table 1). The ongoing rollout of LCR functionality to online and mobile wallet transactions should help to put downward pressure on these scheme fees. The decline in net scheme fees for online debit card transactions in 2023/24 is consistent with this effect.

Table 1: Net Scheme Fees Paid by AcquirersBasis points of transaction values^(a)

	2021/22	2022/23	2023/24
Domestic card transactions			
Debit cards	8.8	9.9	9.5
– Tap/insert card	5.0	5.5	5.3
– Tap device	11.4	12.5	12.8
– Online	13.2	14.3	11.9
Credit cards	12.0	11.9	11.8
International card transactions	157.3	158.0	166.7

(a) Includes scheme fees paid to eftpos, Mastercard and Visa.

Sources: RBA.

For domestic transactions, scheme fees are higher for credit than for debit card transactions. This may partly reflect less competitive tension in the credit card market, relative to the debit market, given that almost all domestic credit cards are issued with Mastercard and Visa, the limited scope for merchants to refuse to accept these two schemes and the absence of any equivalent to LCR. It may be that surcharging, as the main source of competitive pressure, is insufficient to restrain growth in acquirer scheme fees.

Scheme fees are considerably higher for foreign-issued cards than for domestically issued cards.

Scheme fees can also be very complex and opaque. Some card networks have hundreds of fees and their fee schedules typically are not publicly available. Card networks also regularly adjust the level of their fees and add, rename or remove fees. It is unclear whether the complexity of fee schedules is necessary. This complexity means that even acquirers report that they find it difficult to understand the schedules.

The RBA's 2019–2021 Review of Retail Payments Regulation identified a case for greater transparency of card scheme fees to promote competition and help inform merchants. While the RBA has since started collecting scheme fee data and has published some aggregate information, it has been unable to publish data on the fees charged by individual card networks (Connolly 2023). This is because the international card networks did not consent to publication, citing concerns about commercial sensitivity. This prevents market participants and end-users from directly comparing fees across networks.

The RBA seeks feedback on the extent to which these issues are hindering competition and efficiency in the payments system, whether regulatory intervention to address them is warranted and what any intervention should look like. Possible regulatory actions include:

- **Publication of scheme fee data.** To improve price transparency, each designated card network could be required to publish on a quarterly basis the total value of scheme fees collected from issuers and acquirers in Australia (and any rebates provided), along with the volume and value of transactions processed through each network. These data would allow stakeholders to compare the level and growth rates of these fees across networks. Smaller issuers, acquirers and merchants could particularly benefit from greater transparency, because they generally have less bargaining power with the card networks than larger institutions.

Another option would be to require card networks to publish all their multilateral scheme fees and fee-related rules. However, given the complexity of scheme fee schedules and the lack of information on rebates, the publication of aggregate data by the networks may be more effective for promoting competition than requiring networks to publish their multilateral scheme fees and rules.

- **Improved reporting to merchants.** Clear reporting of scheme fees to merchants may help them better understand and check the fees that they are being charged and how they change over time. The RBA is considering options to improve transparency of merchant service fees on merchant statements (see Section 2.5 for further details).
- **Regulation of scheme fees.** The complexity and opacity of scheme fees could be addressed by limiting the number of scheme fees that can be charged or by requiring greater transparency of how pricing decisions are made by the card networks. This could include:
 - consolidating fee categories and standardising fees, which may make it easier for merchants and other stakeholders to understand and compare costs
 - requiring substantive documentation or a formal consultation process with stakeholders to justify new fees or fee increases, which may promote a stronger relationship between scheme fees and the cost of scheme services as is currently being considered by the UK Payment Systems Regulator (2024)
 - implementing caps for scheme fees to limit their growth, equivalent to the current interchange regulations.

For more information on interchange and scheme fees, see the Backgrounder on Interchange and Scheme Fees.

Q4: Is there a case for further transparency of scheme fees to promote efficiency and competition? If so, what additional information would be beneficial?

Q5: Is there a case for regulatory action to reduce the complexity or growth of scheme fees? If so, what form should this take?

Q6: What other regulatory action should the RBA consider to increase the competitive pressure on scheme fees?

2.4. Least-cost routing

Debit cards are now the most frequently used consumer payment method in Australia. Around 85 per cent of debit cards issued in Australia are dual-network debit cards (DNDCs), which allow domestic payments to be processed via either eftpos or one of the international debit networks (Debit Mastercard or Visa Debit). With the advent of contactless technology, transactions using DNDCs defaulted to the international networks that are typically more expensive for merchants. This has resulted in higher merchant card payment costs, which are ultimately borne by consumers either as surcharges or higher overall prices for goods and services.

LCR gives merchants the ability to override the default network and route DNDC transactions via whichever of the two networks on the card costs them less to accept. This can directly reduce card payment costs for merchants while also increasing the competitive pressure on debit networks to lower their wholesale fees, thereby putting downward pressure on payment costs across the economy.

The RBA has been strongly encouraging LCR since 2017. In 2021, in response to slow industry progress, the RBA set an explicit expectation that PSPs offer and promote LCR in both the in-person and online environments. In 2022, the RBA set a further expectation that the industry make LCR functionality available for mobile wallet transactions by the end of 2024. To provide greater transparency on industry progress, in 2023 the RBA started to publish a table on LCR availability and take-up across the major acquirers. By June 2024, the share of merchants with LCR enabled for in-person transactions had increased to around 70 per cent.⁹ Information from PSPs suggests that this proportion should be closer to 80 per cent by the end of 2024. PSPs have also indicated that an

additional 5–10 per cent of merchants have not enabled LCR for arguably valid reasons.¹⁰ As a result, by December 2024, the remaining share of merchants that do not have LCR enabled (without a valid reason provided by their acquirer) is projected to be close to 10 per cent.

LCR for online transactions is at a much earlier stage of progress, with only six of 12 large PSPs having made LCR available to all their merchants by June 2024, and only two providers having LCR enabled for a significant share of their merchants. The online ecosystem is also complex, with the delivery of LCR reliant on intermediaries such as gateways, which has caused some delays. The RBA expects providers, including payment gateways, to accelerate progress on making LCR widely available for online transactions and enabling LCR for merchants that could benefit from it.

An important question is whether the benefits of LCR are being passed on to merchants. The overall take-up of LCR for in-person transactions has been lifted by PSPs offering single-rate merchant payment plans – which charge the same percentage transaction fee for all card types – with LCR implemented ‘in the background’. For merchants on these single-rate plans, LCR serves to lower wholesale costs for PSPs. The extent to which any savings are passed on to merchants will depend on the pricing strategies of PSPs and the degree of competition in the market. Further, the RBA is aware of only one PSP offering a *dynamic* LCR solution – which evaluates and routes each individual transaction to the lowest cost network – while most other PSPs can only offer simple ‘all-or-nothing’ or threshold-based routing solutions, which may limit the potential savings.¹¹

The RBA is interested in views on whether a formal regulatory requirement is warranted for LCR for in-person transactions (excluding mobile wallets), particularly given the progress that has been made to date. For example, PSPs could be required to enable LCR for all merchants by default, with merchants able to opt out if they wish. The RBA is interested in feedback on the benefits, costs and challenges associated with a formal requirement and how it might be designed.

Stakeholder feedback on LCR for online transactions and mobile wallet transactions will be sought in a future phase of the Review given that any formal intervention in these areas would benefit from the passage of the PSRA reforms. Any formal regulatory requirement would probably need to extend to a broader range of PSPs to be effective, such as payment gateways and mobile wallet providers, where there is uncertainty as to whether they are within the scope of the existing PSRA.

For more information on LCR, see the Backgrounder on Least-cost Routing.

Q7: How do stakeholders assess the functioning and effectiveness to date of LCR for *in-person* transactions? Is further regulatory intervention needed? What might that look like?

2.5. Transparency of merchant service fees

In Australia, there is a distinct lack of publicly available information on the merchant service fees, wholesale costs, margins and size of PSPs providing card services to merchants, which may be hampering competition and efficiency in the payments system. This lack of information can make it hard for merchants to compare pricing and switch between PSPs for a better deal and could make it difficult for PSPs to assess their competitors’ offerings. This may be hindering competition between PSPs. In addition, limited public information on wholesale costs may reduce the competitive pressure on card networks to reduce their fees and for PSPs to pass on any reductions in wholesale costs to merchants.

The RBA is considering whether PSPs should be required to publish pricing information to increase transparency and promote competition and efficiency in the card acquiring market. For example, PSPs could be required to publish each quarter their average fees, wholesale costs and margins for merchants by annual transaction volume categories (e.g. under \$100,000; \$100,000 to under \$1 million; and \$1 million and above). While average fees may not be perfectly comparable across PSPs given variation in the services they provide, this information may still help guide merchants towards a cheaper provider or negotiate a better deal with their existing provider. Currently, it can be difficult for merchants to shop around for a better deal because the only publicly available price information provided by most PSPs is for their single-rate or 'simple' merchant plans, where merchants pay the same percentage fee per transaction, irrespective of the type of cards used by their customers. More competitively priced plans are usually negotiated on a bespoke basis between the PSP and the merchant; this is often based on detailed card transaction information that is known to the incumbent PSP but not typically provided to merchants on their standard cost of acceptance statements. Publishing average fees, wholesale costs and margins could help PSPs assess their competitors' offerings and highlight where their services provide additional value. The disclosures would also help policymakers gauge whether any reductions in wholesale costs are being fully passed on to merchants.

Card issuers, card networks and PSPs could be required to publish aggregate information on transaction volumes and values to boost competition and efficiency. While the RBA already collects and publishes some related data in a partially aggregated way (such as Visa and Mastercard's combined market share of credit and charge card transactions), further disaggregation at an institutional level could provide more transparency to the payments market. This would enable stakeholders to identify the most significant players in the industry and to calculate and track changes in market shares.

The RBA is also considering options to improve transparency via the information that merchants receive on their regular statements from acquirers and other PSPs. Currently, some merchants report that they have difficulty understanding and checking the fees they are charged, particularly interchange and scheme fees. It may also be unclear to merchants on single-rate plans how much they are paying for the services their PSP provides over and above the wholesale cost of their transactions. One option to improve transparency for merchants could be to require PSPs to provide a breakdown of the total merchant service fee into interchange fees, scheme fees and their gross margin. PSPs could also be required to provide detailed information on scheme fees by relevant categories (e.g. network, card type, transaction type and issuer location) to merchants. Clear and meaningful information could promote competition between card networks, enable merchants to engage in more informed negotiations with PSPs and help merchants make better decisions on transaction routing. However, additional information could increase the complexity of merchant statements and may add to confusion for some merchants. Accordingly, any requirement to provide information could be made conditional on merchants opting in to receive it. The RBA welcomes views on what information, if any, PSPs should be required to provide that merchants would find useful.

A further potential issue with single-rate plans is that merchants that accept a higher share of debit card transactions effectively cross-subsidise merchants that accept relatively more credit card transactions. The RBA is considering whether, as in some overseas jurisdictions, PSPs should be required to separately price transactions processed across different networks to reduce such cross-subsidisation and to provide more efficient price signals to consumers via surcharging (see Section 2.6 for further details).

The United Kingdom has recently introduced measures to improve transparency and competition in the card acquiring market. These include requiring PSPs to provide merchants with a summary box containing key price and non-price information and to provide an online quotation tool on their website, which allows merchants to compare different providers using the information from their summary boxes (Payment Systems Regulator 2022). The RBA welcomes views on whether similar reforms should be introduced in Australia.

Q8: Is there a case for greater transparency of fees, wholesale costs and market shares for some payment services? If so, what form should this take? What benefits or drawbacks might arise from implementing any of these measures?

Q9: Should PSPs be required to provide individual merchants more detailed information on their regular statements (or through other channels)? How could this information be presented without creating additional complexity for merchants?

Q10: Should PSPs be required to publish standardised information on their pricing and services for merchants (in line with reforms introduced in the United Kingdom)?

Q11: What other regulatory measures should the RBA consider to improve competition between PSPs?

2.6. Surcharging

The RBA seeks feedback on whether and how the issues with surcharging raised in Section 2.1 should be addressed. Possible changes to the RBA's surcharging framework could include, but are not limited to:

- **Banning surcharges on debit transactions.** Preventing merchants from surcharging debit card transactions would help ensure that a surcharge-free electronic payment method is widely available to consumers that is still relatively low cost for merchants. This could help address consumer concerns around the inability to avoid surcharges while maintaining efficient price signalling – at least between debit and credit/charge card transactions – which can help to put downward pressure on card payment costs. It also addresses the desire that consumers be able to access their own funds without a fee. A ban may be practically implemented by allowing card networks to reimpose no-surcharge rules for debit cards. A ban on debit card surcharging may also be easier for consumers and merchants to understand than the current surcharging rules. Such actions may lead PSPs to price debit and credit card transactions differently, which could result in lower wholesale costs for debit cards being passed on to merchants (particularly if consumers continue to shift towards debit cards). However, this could disrupt the business models of PSPs that offer single-rate pricing plans. It may also force merchants who currently surcharge debit cards to absorb the cost of these transactions into their margins or raise their prices; this could then lead to users of other payment methods, such as cash, facing higher prices. Merchants could also seek to reduce their costs by searching for better value payment services.
- **Banning card surcharges more broadly.** A ban on the ability of merchants to surcharge card payments could be applied to all card networks (including charge cards such as American Express) or only those subject to interchange regulation (currently eftpos and Visa and Mastercard's credit, debit and prepaid schemes). This ban could be implemented by reinstating the ability of card schemes to impose 'no-surcharge' rules. Some other jurisdictions, such as the European Union and the United Kingdom, prohibit surcharging for card networks subject to interchange fee caps on the grounds that merchant card payment costs for such schemes are restrained by the interchange rules. However, these jurisdictions often have lower interchange caps than Australia. As above, such a ban would help address consumer concerns about surcharging. It could also give merchants stronger incentives to search for better value payment services. It would also simplify the rules around surcharging, which can be difficult for merchants and consumers to understand. However, this option may unwind the benefits of the existing framework. Prohibiting most or all card surcharges would dull the price signals between payment methods and could drive a shift from cheaper debit transactions towards more expensive credit and charge card transactions (because they offer consumers reward points). This could lead to an overall increase in merchant card payment costs. Merchants may also respond by raising prices for goods and services to cover the costs that were previously recouped through surcharges; consumers who use lower cost payment methods, such as debit cards, would then be

partially subsidising those (typically higher income) consumers who use higher cost payment methods such as credit and charge cards. Finally, the competitive pressure on card networks to keep their scheme fees low may be significantly reduced without surcharging, which could lead to higher card payment costs over time. However, it is worth noting that a ban on card surcharging would not necessarily preclude merchants from offering discounts as a way to incentivise customers to pay with lower cost payment methods.

- **Capping surcharges.** Numerical caps on the level of surcharges could be set for different payment methods. For example, surcharges could be capped at 2 per cent for credit cards and 1 per cent for debit cards. Numerical caps would be much simpler than the current rules and would be easier for the ACCC to enforce (including through consumers holding merchants to account). They could also improve price signalling and reduce a number of consumer concerns, such as excessive surcharging. However, a key challenge would be determining exactly where the caps should be set and how often they should be reviewed. Limits that are too high may lead to higher surcharges and merchant fees, but limits that are too low could prevent some merchants from recouping their payment costs in full through surcharges (particularly smaller businesses).
- **Tightening the definition of the cost of acceptance.** Surcharges could be limited to the pure cost of payment processing, rather than the total 'cost of acceptance', which can include other software services that are bundled into merchant service fees. This could help to both lower surcharges and improve price signalling, but would potentially increase the complexity of the surcharging rules.
- **Mandating differentiated pricing for transactions processed across different networks.** Rather than change the surcharging rules, the RBA could instead mandate differentiated pricing for transactions processed across different networks. This could lead to lower debit surcharges at some merchants, somewhat alleviating consumer concerns, while also improving price signalling. However, as above, this could require significant change from PSPs, especially those that offer single-rate plans.
- **Mandating monitoring of surcharging by networks and acquirers.** To aid visibility over surcharging practices and inform the regulatory response, the RBA has commenced collecting merchant-level data on surcharging from acquirers, terminal providers and other payments software providers. Additional steps the RBA could take to further improve transparency include:
 - requiring card networks to include compulsory data fields on surcharging in transaction messages
 - requiring the networks and/or acquirers to monitor merchant surcharging practices and ensure that surcharges do not exceed the maximum allowed under the RBA's rules.

Such proposals to improve transparency would likely require PSPs to update their systems and may also require the definition of 'cost of acceptance' in the RBA's standard to be narrowed or simplified to just include the costs charged by PSPs.

Q12: Is there a case for revising the RBA's surcharging framework? If so, which options or combination of options would best address the current concerns around surcharging? What other options should the RBA consider?

Q13: What are the implications for merchant payment costs from changes to the surcharging framework? Could the RBA address these with other regulatory actions?

2.7. Other regulatory options and broader implications

The RBA welcomes views from stakeholders on other issues relating to card payments as well as alternative regulatory options to address the issues outlined in this paper. Stakeholders are invited to consider whether a combination of regulatory actions could assist in achieving the RBA's objectives of competition, efficiency and safety in the payments system. The RBA is also interested in views on whether the removal or modification of any of its existing card payments regulation could assist in achieving these objectives.

The RBA recognises that its regulatory actions for card payments potentially have broader implications for other payment methods. Stakeholders are invited to raise whether any of the potential regulatory actions have broader implications for the payments system that the RBA should be aware of. Stakeholders are also invited to raise issues in the broader payments system that have implications for the design of the RBA's policies on card payments. The RBA notes, however, that it may have limited ability to address some issues that are interconnected with merchant card payment costs and surcharging unless the proposed amendments to the PSRA are passed by Parliament.

Q14: Are there any other regulatory actions that the RBA should consider taking in response to the issues raised in this paper?

Q15: Are there any issues in, or implications for, the broader payments ecosystem that the RBA should be aware of when designing a regulatory response to any of the issues discussed in this paper?

Endnotes

- 1 Merchant service fees are comprised of interchange fees, scheme fees and an acquirer margin. Additionally, merchants face other acquiring fees, which are included in 'total merchant fees' for accepting card payments.
- 2 Although the weighted-average interchange benchmarks were maintained following the 2019–2021 Review of Retail Payments, the cap on cents-based interchange fees on debit and prepaid card transactions was reduced to 10 cents, to reduce the cost of low-value transactions at smaller merchants.
- 3 The Federal Reserve Board (2023) has proposed to lower the maximum interchange fee that a large debit card issuer can receive for debit transactions because certain costs incurred by large issuers have declined significantly since 2009, when the original maximum interchange fee was introduced.
- 4 Assumes an average interchange rate for foreign card transactions of 1.75 per cent.
- 5 The number of credit, dual network debit and prepaid interchange categories has increased by around 25 per cent for Visa and more than doubled for Mastercard over the past five years.
- 6 New Zealand's Commerce Commission (2024) considers there to be no reason for a difference in interchange fee rates between transactions where the physical card is present and transactions where it is not.
- 7 Pricing plans can be grouped into three main types: (1) 'unblended' plans charge the merchant the wholesale cost of each transaction (interchange fees and scheme fees) plus an acquirer margin (this is also known as 'interchange plus' or 'interchange plus plus' pricing); (2) 'blended plans' charge a few different rates, each of which may cover a number of networks, card and transaction types; and (3) 'fixed' (or 'simple') plans charge the same rate for all networks, cards and transaction types.
- 8 Brazil simplified its interchange regulations in 2023 for debit transactions by removing the weighted-average cap (0.5 per cent) and lowering the individual cap from 0.8 per cent to 0.5 per cent.
- 9 As at June 2024, the proportion of *transactions* at merchants with LCR enabled (around 50 per cent) was much lower than the proportion of merchants with LCR enabled. This is likely because non-strategic, yet large, institutional merchants account for a sizeable proportion of merchants that do not currently have LCR enabled.
- 10 These include: (1) the merchant has actively chosen not to enable LCR; (2) the acquirer has made an active choice to not enable LCR for the merchant (e.g. because of a difference in capabilities between the domestic and international schemes); and (3) the merchant is sufficiently large and sophisticated to make their own decisions about LCR.
- 11 The 'simple' model involves routing all eligible transactions to one network (usually eftpos); the threshold model routes payments below a certain transaction size to Visa or Mastercard and all other payments to eftpos. This is used because eftpos is usually priced in cents and Visa and Mastercard in percentage terms.

3. Next Steps

3.1. Consultation process and future phases of the Review

Following the release of this issues paper, stakeholders will have seven weeks to make a written submission (see Sections 3.2 to 3.6 for further details). The RBA may reach out to those who make a submission to discuss it in further detail. Stakeholder views from written submissions and discussions will be considered in developing potential regulatory options for the Review.

The RBA will then conduct a public consultation process ahead of any proposed regulatory changes. This will take the form of a consultation paper with detailed analysis of potential regulatory options. The paper is planned for release in 2025, and stakeholders will again be invited to provide written submissions and the RBA will conduct a further round of discussions. The final step will involve a conclusions paper that outlines the decisions made by the PSB and any regulatory changes stemming from these decisions.

Future phases of the broader Review of Retail Payments Regulation will follow a similar process. There are other payments-related issues aside from merchant card payment costs and surcharging that affect the safety, efficiency and competitiveness of the Australian payments system. Examples include, but are not limited to, mobile wallets, online LCR and buy now, pay later products. However, there is uncertainty as to whether the RBA's regulatory remit extends to the relevant industry participants under the existing PSRA. Consideration of these broader issues would be subject to the passage of the amendments to the PSRA that are before the Australian Parliament. Stakeholders wishing to provide views on these matters would be invited to make submissions during subsequent phases of the Review.

3.2. Making a submission

The RBA is seeking views from interested stakeholders on the issues raised in this paper. Written submissions on the issues discussed in Section 2 should be provided by 3 December 2024 to:

pysubmissions@rba.gov.au

or

Head of Payments Policy Department
Reserve Bank of Australia
GPO Box 3947
Sydney NSW 2001

The RBA asks that, where it is practicable to do so, submissions are provided by email.

Submissions provided by email should be in a separate document, in Word or equivalent format. Submissions in PDF format must be accompanied by a version in an accessible format such as .rtf or .doc.

3.3. What happens to submissions

Your submission will be read by RBA staff working on, or involved with, the relevant consultation process to which your submission relates.

In the interests of informed public debate, the RBA is committed to transparency in its processes and open access to information. Accordingly, the RBA aims to publish submissions on its website where it is appropriate to do so. However, the RBA reserves the right to redact (e.g. remove defamatory material or, where appropriate, de-identify personal or sensitive information), publish or not publish submissions on its website at its own discretion. The RBA's publication of a submission is not an indication of the RBA's endorsement of any views or comments contained in that submission.

Most submissions that are published on the RBA website will include the name of the submitter (unless requested otherwise – see Section 3.5). If a submission is published, the information in it, including the submitter's name and any contact details, can be searched for on the internet. You cannot withdraw or alter your submission once the RBA has published it.

3.4. Submissions may be kept confidential

If you do not want some or all of your submission to be published by the RBA, you should clearly indicate this (e.g. by including the word **confidential** prominently on the front of your submission) and provide reasons for your request. Automatically generated confidentiality statements in emails are not sufficient for this purpose.

Where some parts of your submission are considered to be confidential, the RBA requests that you provide two versions of the submission at the same time prior to the closing date – one for consideration by the RBA and one, with confidential information removed, for publication (this latter version may also have contact details or other personal information removed – see Section 3.5).

Please also note that any submission provided to the RBA may be the subject of a request under the *Freedom of Information Act 1982* (Cth). Any request for access to a confidential submission will be determined by the RBA in accordance with that Act, including any applicable exemptions (e.g. those relating to material obtained in confidence or involving an unreasonable disclosure of personal information).

3.5. Privacy

Unless requested otherwise, published submissions will usually include contact details and any other personal information contained in those documents.

Where you provide a separate version of your submission for publication with contact details or other personal information redacted or removed, this will be taken as a request for the RBA not to publish such personal information.

For information about the RBA's collection of personal information and approach to privacy, please refer to the Personal Information Collection Notice for Website Visitors and the RBA's Privacy Policy, which are both available at [Privacy](#).

3.6. Intellectual property rights

In making a submission to the RBA, you grant a permanent, irrevocable, royalty-free licence to allow the RBA to use, reproduce, publish, adapt and communicate to the public your submission on the RBA's website (except to the extent that you have specifically requested that all or part of your submission is kept confidential), including converting your submission into a different format to that submitted for the purposes of meeting relevant accessibility requirements.

To the extent that your submission contains material that is owned by a third party, you warrant that you have obtained all necessary licences and consents required for the use of those materials (including for the RBA to use, reproduce, publish, adapt or communicate to the public such material), and have made arrangements for the payment of any royalties or other fees payable in respect of the use of such material.

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Appendix A: Questions for Stakeholders

1. **Is there a case for lowering the level of interchange benchmarks or caps? Should the difference between the interchange fees paid by big and small businesses be limited in some way?**
2. **Should interchange regulation be extended to foreign card transactions in Australia?**
3. **Is there a case for reducing the complexity, and/or enhancing the transparency, of interchange fees? If so, how?**
4. **Is there a case for further transparency of scheme fees to promote efficiency and competition? If so, what additional information would be beneficial?**
5. **Is there a case for regulatory action to reduce the complexity or growth of scheme fees? If so, what form should this take?**
6. **What other regulatory action should the RBA consider to increase the competitive pressure on scheme fees?**
7. **How do stakeholders assess the functioning and effectiveness to date of LCR for *in-person* transactions? Is further regulatory intervention needed? What might that look like?**
8. **Is there a case for greater transparency of fees, wholesale costs and market shares for some payment services? If so, what form should this take? What benefits or drawbacks might arise from implementing any of these measures?**
9. **Should PSPs be required to provide individual merchants more detailed information on their regular statements (or through other channels)? How could this information be presented without creating additional complexity for merchants?**
10. **Should PSPs be required to publish standardised information on their pricing and services for merchants (in line with reforms introduced in the United Kingdom)?**
11. **What other regulatory measures should the RBA consider to improve competition between PSPs?**
12. **Is there a case for revising the RBA's surcharging framework? If so, which options or combination of options would best address the current concerns around surcharging? What other options should the RBA consider?**
13. **What are the implications for merchant payment costs from changes to the surcharging framework? Could the RBA address these with other regulatory actions?**
14. **Are there any other regulatory actions that the RBA should consider taking in response to the issues raised in this paper?**
15. **Are there any issues in, or implications for, the broader payments ecosystem that the RBA should be aware of when designing a regulatory response to any of the issues discussed in this paper?**

Backgrounder on the RBA's Current Payments Regulations

Overview

Under the *Payment Systems (Regulation) Act 1998* (PSRA), the RBA may designate a payment system if it considers that designating the system is in the public interest. It may then impose an access regime or establish standards that participants in the system must comply with:

- Access regimes set out rules with respect to participants ability to join designated payment systems.
- Standards determined by the RBA to date have generally set out rules that relate to the governance or operation of designated payments systems and the conduct of participants within those systems.

Some organisations have provided written undertakings to the RBA in relation to standards determined under the PSRA or certain policy concerns relating to efficiency and competition in the Australian payments system. Undertakings are commitments made by organisations to the RBA about conduct in relation to payments systems.

This Backgrounder lists the designations, access regimes, standards, undertakings, guidance and exemptions as at October 2024 relevant to the regulation of the payments system.

Card regulation

Designations

The objective of designating a payment system is to allow the RBA to impose an access regime on, or establish standards for, that payment system if it considers that doing so is in the public interest. The RBA has imposed instruments prescribing access regimes and/or specific standards for the following designated card payment systems.

Designation of system	Title	Commencement date	Date of gazettal	Media release
MasterCard (credit)	Designation of MasterCard system	12 Apr 2001	12 Apr 2001	2001-09
Visa (credit)	Designation of VISA system	12 Apr 2001	12 Apr 2001	2001-09
Visa Debit	Designation of Visa debit	23 Feb 2004	23 Feb 2004	2004-01
EFTPOS (debit)	Designation No.1 of 2012	12 Jun 2012	12 Jun 2012	2012-15
Debit MasterCard	Designation No.2 of 2015	15 Oct 2015	15 Oct 2015	2015-19
EFTPOS prepaid	Designation No.3 of 2015	15 Oct 2015	15 Oct 2015	2015-19
MasterCard prepaid	Designation No.4 of 2015	15 Oct 2015	15 Oct 2015	2015-19
Visa prepaid	Designation No.5 of 2015	15 Oct 2015	15 Oct 2015	2015-19

Access regimes

The objective of the following access regimes is to promote efficiency and competition among payment service providers in the Australian payments system.

These access regimes place limitations on the types of restrictions scheme operators can place on scheme membership eligibility and on the credit card acquiring activity of members. The amendments introduced in 2015 provided the card systems with the flexibility to expand membership beyond existing participants. The card systems are required to have in place transparent eligibility and assessment criteria and to report information about membership and applications to the RBA.

System	Title	Commencement date	Date of gazettal	Media release
Mastercard (credit)	Access Regime	23 Feb 2004	23 Feb 2004	2004-02
			Variation: 1 Jan 2015	2014-22
Visa (credit)	Access Regime	23 Feb 2004	23 Feb 2004	2004-02
			Variation: 1 Jan 2015	2014-22

Interchange fees

Objective

The objective of the RBA's interchange standards is to ensure that the setting of interchange fees and other transfers in card schemes is transparent and promotes efficiency and competition in the Australian payments system. The standards limit interchange fees in designated card payment systems, with the aim of reducing payment costs to merchants.

Regulations

System	Title	Commencement date	Date of gazettal/ registration	Media release
MasterCard (credit) Visa (credit)	Standard No.1 of 2016: The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers (compilation)	1 Jul 2017, amended effective 1 Jan 2022	26 May 2016	2016-15
			Variation: 21 Nov 2017	2017-24
			Variation: 3 June 2019	2019-14
			Variation: 18 Nov 2021	2021-23
Visa Debit EFTPOS (debit) Debit MasterCard EFTPOS prepaid MasterCard prepaid Visa prepaid	Standard No.2 of 2016: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers (compilation)	1 Jul 2017, amended effective 1 Jan 2022	26 May 2016	2016-15
			Variation: 21 Nov 2017	2017-24
			Variation: 3 June 2019	2019-14
			Variation: 18 Nov 2021	2021-23

Guidance

The RBA has provided the following guidance on the above standards to support a consistent interpretation of some terms and clarity around the RBA's views and expectations on related issues. This guidance is not a substitute for parties obtaining their own legal advice.

System	Title	Date
All designated systems	Guidance on 'Core Services' in Standard No.1 of 2016 and Standard No.2 of 2016	29 Apr 2020
All designated systems	Guidance for new Issuers on certification under Standard No.1 of 2016 and Standard No.2 of 2016	25 Feb 2021

Net compensation

Objective

The following standards apply to designated card schemes and place limits on non-interchange payments to issuers ('net compensation'). The objective is to prevent circumvention of the limits on interchange fees by arrangements involving non-interchange payments or other incentives being provided by schemes to issuers.

Regulations

System	Title	Commencement date	Date of gazettal/ registration	Media release
MasterCard, Visa	Standard No.1 of 2016: The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers (compilation)	1 Jul 2017, amended effective 1 Jan 2022	26 May 2016	2016-15
			Variation: 21 Nov 2017	2017-24
			Variation: 3 June 2019	2019-14
			Variation: 18 Nov 2021	2021-23
Visa Debit, EFTPOS, Debit MasterCard, EFTPOS prepaid, MasterCard prepaid, Visa prepaid	Standard No.2 of 2016: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers (compilation)	1 Jul 2017, amended effective 1 Jan 2022	26 May 2016	2016-15
			Variation: 21 Nov 2017	2017-24
			Variation: 3 June 2019	2019-14
			Variation: 18 Nov 2021	2021-23

Guidance

The RBA has provided the following guidance on the above standards setting out an expectation that issuing contracts contain a methodology for valuing non-monetary benefits, for the purpose of making assessing compliance with the net compensation provisions more straightforward.

System	Title	Date
All designated systems	Guidance on the valuation of non-monetary benefits under Standard No. 1 of 2016 and Standard No. 2 of 2016	6 Apr 2022

Surcharging and merchant pricing

Objective

The objective of the following surcharging regulations and merchant pricing undertakings is to promote efficiency and competition by promoting scheme rules that allow merchants to charge an amount for accepting a payment method that reflects the merchant's cost of acceptance for that payment method.

Regulations

System	Title	Commencement date	Date of gazettal/ registration	Media release
All designated systems	Standard No.3 of 2016: Scheme Rules Relating to Merchant Pricing for Credit, Debit and Prepaid Card Transactions (compilation)	1 Sep 2016, amended effective 1 Jan 2022	26 May 2016	2016-15
			Variation: 18 Nov 2021	2021-23

Undertakings

System	Title	Commencement date	Media release
UnionPay	Undertaking No.1 of 2019: Merchant Pricing for UnionPay Card Transactions	1 Oct 2019	
American Express	Undertaking No.3 of 2016: Merchant Pricing for American Express Proprietary Card Transactions	2 Sep 2016	2002-15

System	Title	Commencement date	Media release
Diners Club	Undertaking No.4 of 2016: Merchant Pricing for Diners Club Card Transactions	14 Oct 2016	2002-15

Honour all cards

Objective

The objective of the following 'Honour All Cards' undertakings is to promote competition and efficiency by allowing merchants to choose which cards they accept.

Undertakings

System	Title	Commencement date
MasterCard Credit, Debit and Prepaid	Undertaking No.1 of 2016: The 'Honour All Cards' Rule in the Designated MasterCard Credit, Debit and Prepaid Systems	1 Sep 2016
VISA Credit, Debit and Prepaid	Undertaking No.2 of 2016: The 'Honour All Cards' Rule in the Designated Visa Credit, Debit and Prepaid Systems	1 Sep 2016

Least-cost routing

Objective

The schemes listed below have given the following voluntary undertakings that they will not engage in 'tying' conduct by making preferential 'strategic' interchange rates on credit card transactions conditional or 'tied' to the value or volume of a merchant's debit card transactions. The objective of these undertakings is to address concerns that such conduct could limit competitive pressure in the debit card market, which has the potential to impose additional costs on the payments system.

Undertakings

System	Title	Commencement date	Media release
Mastercard	Undertaking No.1 of 2023: Mastercard Undertaking In Relation to Least-Cost Routing of Debit Transactions by Merchants	1 Jul 2023	2023-15
Visa	Undertaking No.2 of 2023: Visa Undertaking In Relation to Least-Cost Routing of Debit Transactions by Merchants	1 Jul 2023	2023-15

ATM system regulation

ATM access regime

Objectives

The following ATM access regime was introduced in 2009 as part of a broader set of industry-led reforms aimed at promoting efficiency and competition in the ATM market. Its primary objectives are to:

- increase competition in the ATM system by making it easier for firms to enter
- introduce greater competition in ATM fees by removing the inflexible and opaque interchange arrangements and transitioning the industry to a more transparent direct charging model where ATM owners can set their own fees and compete for transactions
- increase ATM deployment by giving ATM owners the flexibility to reflect the cost of deployment in the fees they charge.

Regulations

Title	Commencement date	Date of gazettal	Media release
Designation	10 Dec 2008	10 Dec 2009	2008-28
Access Regime (Compilation)	3 Mar 2009	24 Feb 2009	2009-03
		Variation: 29 Aug 2012	2012-24

Exemptions

The RBA may grant an exemption to a participant in the ATM system from any or all of the requirements of paragraphs 11 and 12 of the ATM access regime in accordance with paragraph 16 of the regime. The following exemptions have been granted.

Exemption number	Description	Commencement date
No 1 of 2009	Arrangement between Cashcard Limited and Bank of Western Australia Limited in relation to Commonwealth Bank of Australia.	16 Jul 2009
No 1 of 2012	Arrangement among ATM industry participants in relation to ATM access for very remote Indigenous communities.	29 Aug 2012
	Consent in relation to Exemption No 1 of 2012	1 Dec 2017
No 1 of 2017	Arrangement between Indue Limited, Westpac Banking Corporation and DC Payments Limited in relation to balance enquiries by holders of Cashless Debit Cards.	1 Jan 2017
No 1 of 2021	Exemption allowing ATM participants to enter into multiple one-way arrangements.	19 Oct 2021

Regulation of purchased payment facilities

Under Part 4 of the PSRA, the RBA has regulatory responsibilities in respect of purchased payment facility (PPF) providers, except where provision of a PPF has been determined to be banking business under Regulation 6 of the Banking Regulation 2016 (providers of such PPFs are required to be authorised and supervised by APRA). The RBA may authorise a corporation to be the holder of stored value of a PPF under section 23 of the PSRA. To date, the RBA has not authorised any corporation under section 23. Under subsection 9(3) of the PSRA, the RBA may declare that the PSRA does not apply to a specified PPF or to facilities included in a specified class of facilities. The RBA may also exempt corporations under section 25 of the PSRA. Such an exemption allows them to be the holders of the stored value in respect of PPFs, even though they are not authorised deposit-taking institutions (ADIs) and do not hold an authority under section 23 of the PSRA that covers those facilities. The following declarations and exemptions have been made.

Declarations under subsection 9(3): Exempt purchased payment facilities

Number	Facility	Date of gazettal	Media release
No. 1 of 2006	Loyalty schemes (ASIC CO 05/737)	27 Apr 2006	2006-02
	Gift card facilities (ASIC CO 05/738)		
	Electronic road toll devices (ASIC CO 05/739)		
	Pre-paid mobile phone accounts (ASIC CO 05/740)		
No. 2 of 2006	Limited-value (\$10,000,000)	27 Apr 2006	2006-02
	Limited-participant (50 persons)		
No. 1 of 2012	Westfield insurance card facility	10 Oct 2012	

Exemptions under section 25: Holders of stored value

Coverage of exemption	Date of gazettal	Media release
Corporations guaranteed by an ADI or government authority	10 Mar 2004	2004-04

Backgrounder on Interchange and Scheme Fees

Overview

When people use their credit or debit card to buy goods and services, there are a detailed set of arrangements between financial institutions and payment service providers (PSPs) that ensure that the merchant is paid and the cardholder's account is debited as intended. As part of these arrangements, the merchant's PSP pays fees to the cardholder's bank (card issuer). These fees are known as 'interchange fees'. While interchange fees are most common in card transactions, they can also arise in other payment methods. Both the merchant's PSP and the card issuer also pay fees to the card scheme. These fees are known as 'scheme fees'. PSPs recoup from merchants the interchange and scheme fees they pay, by charging them fees for the payment services they provide.

This Backgrounder describes interchange and scheme fees and explains interchange fee regulation in Australia as at October 2024.

What is an interchange fee?

A typical card transaction involves four parties – the cardholder, the card issuer,¹ the merchant and the merchant's payments provider (the acquirer) (Figure 1). Interchange fees are typically paid by the acquirer to the issuer every time a payment is made.²

Interchange fees are typically set by the operators of payment networks, such as Visa or Mastercard, for payment card schemes. These fees can vary based on factors like the type of card, whether it is an online or in-person transaction, the value of the transaction and the size of the merchant. For example, cards that provide rewards to the cardholder (such as 'gold' or 'platinum' credit cards) have higher interchange fees. While card schemes publish interchange fees on their websites, many cardholders and merchants are not aware of them. But they have an impact on the fees that cardholders and merchants pay.

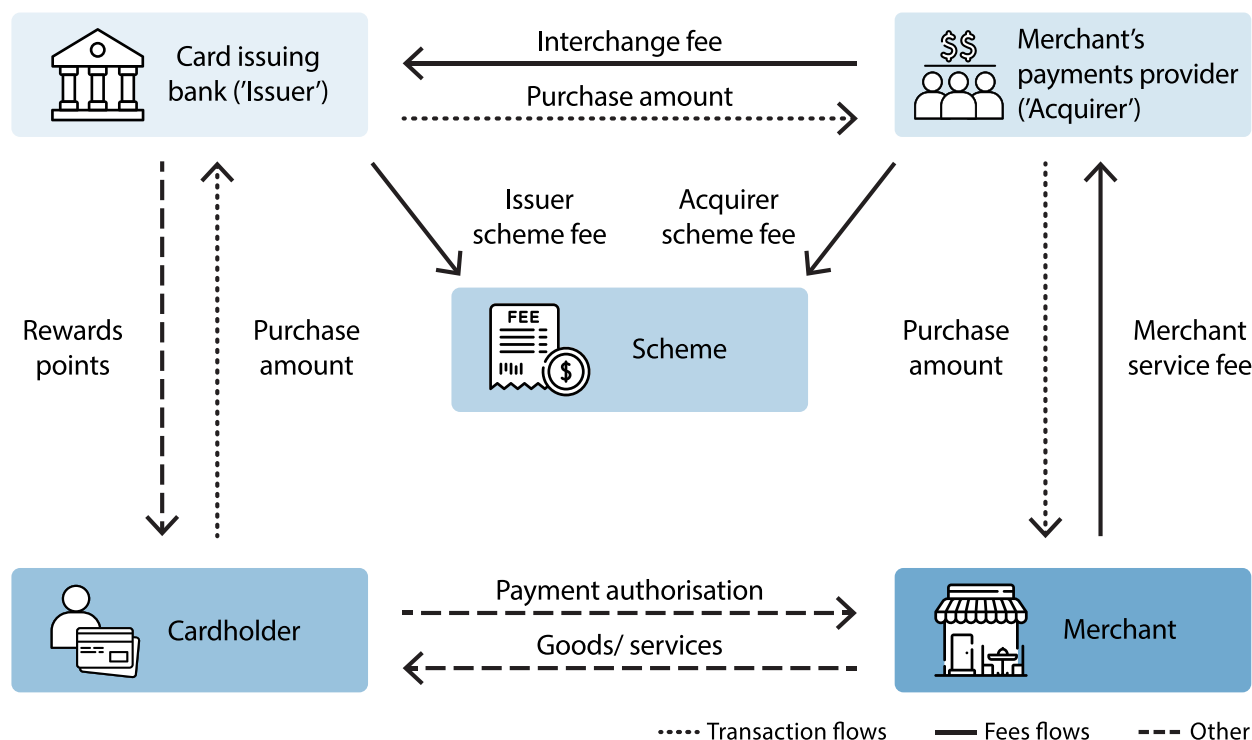
Why do interchange fees exist?

Interchange fees can help establish new payment systems. New payment networks or technology often face a classic 'chicken and egg' problem when starting out – merchants do not want to invest in accepting new payment type until enough consumers have adopted it and consumers do not want to use a new payment type until enough merchants accept it. Interchange fees can help to rebalance costs between each side of the market and ensure that both sides of the market have an incentive to participate. For example:

- Revenue from interchange gives card issuers more motivation to issue payment cards/accounts on the new network to their customers.
- Revenue from interchange can be used to fund consumer rewards programs that incentivise usage.
- Revenue from interchange helps pay for building infrastructure, operations and new features, such as additional security.

Why do interchange fees matter?

When a card payment is made, interchange fees are paid by the merchant's payment provider to the cardholder's card issuer.³ This has two effects:



Source: RBA.

- The merchant's payments provider passes on the cost of the interchange fee to the merchant. So, the higher the interchange fee, the more the merchant will have to pay to accept a card payment.
- Since the card issuer receives the interchange fee every time its card is used, it does not need to charge its customer – the cardholder – as much. In effect, the merchant is meeting some of the card issuer's costs, which ultimately benefits the cardholder. With rewards programs, the cardholder may receive more in benefits through rewards than what it costs them to use the card.

Interchange fees can have important implications for the prevalence and acceptance of different cards as well as the relative costs faced by consumers and merchants. A network that increases the interchange fee paid by the merchant's payments provider to the card issuer enables the latter to pay more generous rewards to cardholders and increase use of its cards. However, if the network is mature (i.e. widely used by consumers and accepted by merchants across the economy), merchants may feel that they have little choice but to continue accepting the network's cards, despite the higher cost. A logical competitive response from other mature networks is to increase their interchange rates as well. So, in contrast to normal markets for goods and services, competition in well-established payment card networks can lead to the counterintuitive result of *increasing* the price of payment services to merchants (and thereby leading to either higher retail prices for consumers and/or higher surcharges).

As the major card schemes are mature systems, regulators in many countries have concluded that their cards are 'must take' methods of payments – that is, merchants have little choice but to accept their cards if they want to attract and retain customers. In practice, competition between these mature card schemes has driven up interchange fees and costs to merchants. As a result, regulators in many jurisdictions, including Australia, have introduced rules to cap interchange fees.

What rules apply to interchange fees in Australia?

Since the early 2000s, the RBA has introduced several reforms aimed at lowering payment costs.⁴ This has included rules to reduce the size of interchange fees. Other reforms have allowed merchants to surcharge, which has helped to provide accurate price signals to customers and, in turn, increase competitive pressure on the fees charged to merchants.⁵ The reforms have led to a lower cost payment system overall.

In short, the current interchange fee regulations:

- cap credit card interchange fees to a weighted average of 0.50 per cent of transaction value, with a ceiling on individual interchange rates of 0.80 per cent⁶
- cap debit card and prepaid card interchange fees to a weighted average of 8 cents per transaction (for all debit and prepaid cards) with a ceiling on individual interchange rates of 10 cents, or 0.20 per cent if specified in percentage terms.⁷

What is a scheme fee?

Scheme fees are charged by card schemes – such as Visa, Mastercard and eftpos – to acquirers and issuers for the services they provide (Figure 1). These fees can include:

- **Assessment fees** – used to cover the costs of operating and maintaining the card network’s infrastructure.
- **Processing fees** – charged for processing and authorising transactions.
- **Licensing and access fees** – charged for use of the network and its brand.
- **Other fees** – charged for discrete services such as chargebacks, security features, new technologies, compliance and currency conversion.

Why do scheme fees matter?

Scheme fees matter because they are an important component of the overall costs faced by merchants to accept card payments, as well as the costs borne by issuers for providing card services to their customers. These costs are ultimately passed on to consumers.

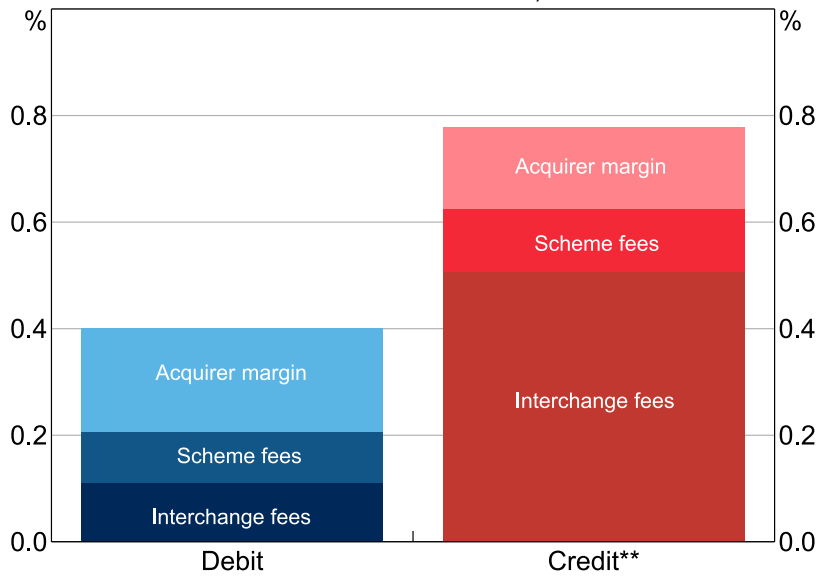
Scheme fee schedules are often complex with fees being set based on commercial considerations, and are currently not directly regulated in Australia. The RBA is not aware of scheme fees being directly regulated in other countries.⁸ However, following the RBA’s Review of Retail Payments Regulation in 2021, the RBA has been collecting information and data on scheme fees and exploring possible scheme fee disclosure requirements to provide greater transparency of scheme fees to participants in the payment system.⁹

The size of interchange and scheme fees in Australia

Interchange fees and scheme fees explain around half of the debit card costs for merchants and most of their credit card costs. The remainder is the gross margin that acquirers and other PSPs charge merchants (Graph 1).¹⁰

Merchant fees have decreased over the past 20 years, supported by regulatory interventions by the RBA. However, the cost of card payments is substantial for small businesses, which pay much higher fees per transaction than large businesses. Large merchants have the bargaining power to directly negotiate much lower ‘strategic’ interchange rates from the networks. They also benefit from lower payment costs due to economies of scale (Graph 2).

Graph 1
Average Merchant Fees of Card Payments*
 Per cent of transaction values, 2023/24

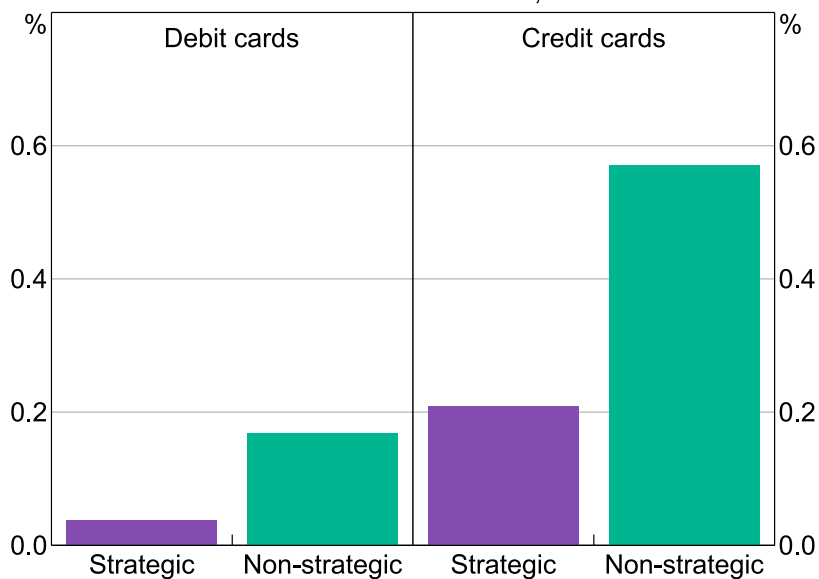


* Domestic card transactions. The acquirer margin component is estimated as the difference between average merchant fees and wholesale costs (the sum of average interchange and scheme fees).

** Mastercard and Visa Credit only. Interchange fee component is calculated by taking each scheme's weighted average credit interchange rate and weighting those rates by the number of transactions for each scheme.

Source: RBA.

Graph 2
Domestic Interchange Fees by Merchant Type*
 Per cent of transaction values; 2023/24



* Strategic interchange fees are available for typically larger merchants who meet certain requirements (e.g. volume requirements) as defined by the schemes.

Source: RBA.

Net scheme fees of around \$1.8 billion were paid by Australian acquirers and issuers to the card networks in 2023/24 (Table 2). The fees paid by issuers are much lower than those paid by acquirers because issuers receive significant rebates from schemes competing for their card issuing business. As a result, most of the burden of scheme fees falls on acquirers, which then gets passed on as higher costs for merchants.

Table 2: Net Scheme Fees
Basis points of transaction values^(a)

	2021/22	2022/23	2023/24
Domestic card transactions			
<i>Acquirers</i>	9.9	10.6	10.3
Debit cards	8.8	9.9	9.5
– Tap/insert card	5.0	5.5	5.3
– Tap device	11.4	12.5	12.8
– Online	13.2	14.3	11.9
Credit cards	12.0	11.9	11.8
– Tap/insert card	11.0	11.2	11.6
– Tap device	12.0	12.3	13.3
– Online	12.6	12.2	11.6
<i>Issuers</i>	2.8	3.0	3.0
Debit cards	2.2	2.6	2.5
Credit cards	3.8	3.7	3.7
International card transactions			
<i>Acquirers</i>	157.3	158.0	166.7
<i>Issuers</i>	44.4	64.5	28.2

(a) Includes scheme fees paid to eftpos, Mastercard and Visa.

Source: RBA.

Endnotes

- 1 The issuer is usually a bank but can sometimes be a non-bank financial institution.
- 2 An alternative card scheme model is the 'three-party' scheme, which involves the merchant, the cardholder and scheme. In this model, the scheme fulfils the role of both issuer and acquirer, providing card acceptance services and charging merchant service fees to merchants while collecting funds from – and charging fees, interest (if applicable) and offering rewards to – cardholders. In such a three-party scheme, no interchange fees apply. As a result, three-party schemes, such as American Express, are not subject to the RBA's interchange regulation.
- 3 RBA (2019), 'Box A: Interchange Fees and Surcharging: Key Concepts', Review of Retail Payments Regulation Issues Paper, November.
- 4 Bullock M (2010), 'A Guide to the Card Payments Reforms', September.
- 5 For further information on surcharging, see RBA (2024), 'Backgrounder on Payment Surcharges in Australia', October.
- 6 RBA (2016), 'The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers', Standard No 1.
- 7 RBA (2016), 'The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers', Standard No 2.
- 8 In 2002, the People's Bank of China imposed a '8:1:1 rule' cap, setting the division of the merchant fee between interchange, switch fees and acquirer fees respectively: see Federal Reserve Bank of Kansas City (2024), 'Public Authority Involvement in Payment Card Markets: Various Countries', August.
- 9 RBA (2021), 'Chapter 5: Scheme Fees', Review of Retail Payments Regulation Conclusions Paper, October.
- 10 Connolly E (2024), 'Online Retail Payments – Some Policy Issues', Speech at the Merchant Risk Council Conference, Melbourne, 18 June.

Backgrounder on Least-cost Routing

Debit card transactions in Australia

Debit cards are used in around half of all payments made by consumers in Australia. When a merchant (e.g. a shop or business) accepts a payment from a customer using a debit card, the merchant is charged a fee by their card issuer or payments provider. Higher payments costs for merchants feed through into higher prices for goods and services.

In Australia, around 85 per cent of debit cards are 'dual-network' debit cards (DNDCs), which allow domestic payments to be processed by either eftpos (the domestic card network) or one of the international debit networks (Debit Mastercard or Visa Debit). These cards have an international scheme logo (Mastercard or Visa) on one side and the eftpos logo on the other. A payment made with a DNDC draws on the same deposit account, regardless of which card network processes it. But the cost the merchant faces from their payment service provider (PSP) for accepting a debit card payment can vary depending on which of the card networks processes the transaction.

When a customer makes a contactless payment by tapping their DNDC on a terminal, the transaction would be automatically routed to the default network programmed on the card, which is typically the Debit Mastercard or Visa Debit network. However, for many merchants, payments via the eftpos network can be less expensive than payments via the Debit Mastercard or Visa Debit networks because the eftpos network has lower wholesale costs. The increasing use of contactless functionality by consumers has put upward pressure on the costs to merchants for accepting debit transactions. As a result, the RBA has strongly supported the introduction of functionality known as least-cost routing (LCR).

This Backgrounder describes LCR and its impact on payment costs.

What is least-cost routing?

LCR provides merchants the ability to override the default network and route contactless DNDC transactions via whichever of the two networks on the card costs them less to accept. Routing transactions via the international networks may be cheaper for some merchants, particularly those with low average transaction values, because PSPs typically charge a percentage rate for the international networks and a cents-based fee for eftpos. But having LCR enabled does not necessarily mean that transactions are always routed to eftpos.

In practice, LCR is implemented in the following ways:

- *Binary LCR* – all eligible transactions are routed to one network, chosen by the merchant (or PSP).
- *Threshold LCR* – the merchant (or PSP) chooses a threshold transaction value so that transactions with a value below the threshold are routed to one network, while transactions with a value above the threshold are routed to the other network. This reflects the fact that the lowest cost network may vary across transactions of different sizes.
- *Dynamic LCR* – the lowest cost network is assessed and chosen for each individual transaction. This reflects the fact that the lowest cost network may vary across transactions, due to factors such as transaction value. Dynamic LCR is not yet widely available because it is more complex and so the technology is harder for PSPs to implement.¹

What is the availability and take-up of least-cost routing?

LCR is widely available for in-person contactless ('tap and go') transactions made with a physical debit card. LCR also started to become available for online transactions following eftpos launching online payments functionality in 2022. Previously, online debit card payments could only be processed via the international networks (Visa Debit or Debit Mastercard). The RBA expects LCR to become available for mobile wallet transactions by the end of 2024.

Merchants that do not have LCR enabled can either ask their PSP about the availability of LCR and how to enable it, or switch to a pricing plan with LCR enabled. To provide greater transparency on the extent to which providers are supporting LCR, the RBA publishes tables on LCR availability and take-up across the major acquirers.²

How can least-cost routing reduce payment costs?

LCR helps to reduce payment costs in the following ways:

- It gives merchants and PSPs the ability to route DNDC transactions to the lowest cost network, which directly reduces their payment costs. For merchants on plans with blended pricing across debit and credit (or across debit schemes), LCR serves to lower wholesale costs for PSPs. The extent to which any savings are passed on to merchants will depend on the pricing strategies of PSPs and the degree of competition in the market.
- It increases the competitive pressure on the debit card networks to lower the wholesale fees – known as interchange fees and scheme fees – that they set on debit card transactions.³ These fees are a key component of the price that merchants pay to accept card payments.

The RBA has estimated that the cost of accepting debit card transactions is nearly 20 per cent lower for merchants with LCR, although the results differ across merchant size and type of pricing plan. Once LCR for online and mobile wallet payments is widely available and taken up by merchants, the potential cost savings are likely to be even larger.⁴

What is the RBA doing to support least-cost routing?

The RBA has a mandate to promote competition, efficiency and safety in the Australian payments system. As such, the RBA has strongly encouraged availability of LCR since 2017:

- In 2021, in response to slow industry progress, the RBA set an explicit expectation that PSPs offer and promote LCR in both the in-person and online environments.⁵
- In 2022, the RBA set a further expectation that the industry make LCR functionality available for mobile wallet transactions by the end of 2024.⁶
- To provide greater transparency on industry progress, the RBA started to publish in 2023 a table on LCR availability and take-up across the major acquirers.⁷
- By June 2023, LCR was widely available to merchants for in-person transactions, but the functionality had only been enabled for just over half of merchants. In addition, only a few acquirers and other PSPs had made LCR available to their merchants for online transactions. As a result, the RBA communicated that if 'substantial progress' was not made by June 2024, it would explore a formal regulatory requirement for PSPs to enable LCR for merchants by default.⁸

By June 2024, the share of merchants with LCR enabled for in-person transactions had increased to around 70 per cent, with PSPs indicating that they would make further progress by the end of 2024. However, LCR for online transactions is at an earlier stage of progress as the industry is still adjusting to the rollout of eftpos's online functionality. Only six of 12 large PSPs had made LCR available to all their merchants by June 2024, and two providers had LCR enabled for a significant share of their merchants.⁹

The RBA is also exploring if further regulatory action may be needed to realise the full benefits of LCR for in-person transactions.¹⁰ For example, the RBA is considering whether PSPs should be required to enable LCR for all merchants by default, with merchants able to opt out if they wish. The RBA is also planning to seek stakeholder feedback on LCR for online transactions and mobile wallet transactions at a later time. Online and mobile LCR are at an earlier stage of progress and any formal intervention in these areas would benefit from the passage of proposed reforms to the *Payment Systems (Regulation) Act 1998* that would broaden the definition of ‘participants’ in payment systems to include service providers such as mobile wallets and payment gateways.

Endnotes

- 1 Gill T, C Holland and G Wiley (2022), ‘The Cost of Card Payments for Merchants’, *RBA Bulletin*, September.
- 2 See RBA (2024), ‘Update on Availability and Enablement of Least-cost Routing for Merchants’, August.
- 3 For further information on these fees, see ‘Backgrounder on Interchange and Scheme Fees’.
- 4 Dobie B and B Watson (2024), ‘The Effect of Least-cost Routing on Merchant Payment Costs’, *RBA Bulletin*, April.
- 5 See RBA (undated), ‘Least-cost Routing of Debit Card Transactions’.
- 6 See RBA, n 5.
- 7 See RBA, n 2.
- 8 Payments System Board (2023), ‘Payments System Board Update: August 2023 Meeting’, Media Release No 2023-20, 17 August.
- 9 Payments System Board (2024), ‘Payments System Board Update: August 2024 Meeting’, Media Release No 2024-16, 15 August.
- 10 The RBA commenced a review of merchant card payment costs and surcharging in October 2024.

Backgrounder on Payment Surcharges in Australia

What is a payment surcharge?

A payment surcharge is a fee paid by customers, in addition to the price of a good or service, allowing merchants to pass on the cost of the customer's chosen payment method.

This Backgrounder describes the current surcharging framework that applies to payment surcharges in Australia, the impact of surcharges on consumers and the approach taken to surcharges in other jurisdictions.

What are the rules about surcharging in Australia?

Currently, merchants have the right to apply a surcharge on card payments, but this surcharge is limited to the amount it costs the merchant to accept that type of card for that transaction. There are three key elements to the surcharging framework, which are broadly as follows:

1. Card acceptance costs are limited to fees paid to the merchant's payment service provider (acquirer or payments facilitator) and other observable costs paid to third parties for services directly related to accepting particular types of cards.
2. Payment service providers must provide merchants with an annual statement that clearly sets out their average cost of acceptance for each of the card payment systems regulated by the RBA. Acceptance costs must be expressed as a percentage of transactions.¹ Merchants need to calculate for themselves any other observable costs paid to third parties and that are directly relatable to accepting particular cards.
3. The *Competition and Consumer Act 2010* (Cth) prohibits merchants from applying excessive card payment surcharges – this is defined as charging a higher amount than what it costs the merchant to use any particular card payment type. The Australian Competition and Consumer Commission (ACCC) has powers to investigate and take enforcement action in the case of possible excessive surcharging.

The Australian Consumer Law (ACL), enforced by the ACCC along with state and territory consumer protection agencies, includes requirements which mean that merchants need to provide clear pricing to customers. The merchant must not mislead customers about their prices and must display the minimum total cost of a product or service, inclusive of any unavoidable or preselected fees.

The ACL also requires:

- merchants to display any surcharges prominently so that consumers are aware of any potential additional costs before payment
- merchants to include the minimum surcharge in the total single figure price displayed for any product or service if they do not provide a surcharge-free payment method.

Why did the RBA implement a surcharging framework?

RBA's surcharging framework aims to lower payment costs for merchants, which, in turn, flows through to lower prices for consumers. Merchants incur costs when they accept a payment from a customer. Different payment methods can have different costs. For example, in 2023, the average cost of a debit-card transaction was around

0.4 per cent, a credit card transaction was around 0.8 per cent, and a charge card transaction was around 1.3 per cent. Unlike other costs that merchants face, such as rent or electricity, a customer's choice to pay with one method over another affects the costs faced by the merchant.

When customers can see the costs associated with their chosen payment method, it puts competitive pressure on payment service providers and payment system operators. If the prices of payment services are set too high, customers may choose a cheaper alternative. This incentivises payment service providers and payment system operators to keep their fees low. However, if customers do not directly see the cost of their chosen payment method, they may gravitate towards higher cost payment methods that include more benefits targeted at customers (e.g. rewards points). For merchants to recover these higher costs, they need to raise overall prices, leading to higher prices for *all* customers, even those who pay using lower cost payment methods.

How many card payments are surcharged?

Data available to the RBA suggest that surcharging has increased in recent years, but apply only to a minority of total card purchases by consumers. In the 2022 Consumer Payments Survey, respondents reported that 7 per cent of all card payments attracted surcharges, an increase from around 5 per cent in 2019. The low share of transactions that attracted surcharges partly reflects that large, frequently visited merchants such as supermarkets, large online retailers, petrol stations and large fast-food chains typically do not apply surcharges. Data from one payment service provider suggests that there has been an increase in the prevalence of surcharging in recent years, particularly in hospitality, with around half of this provider's merchants in the hospitality industry surcharging in mid-2023.²

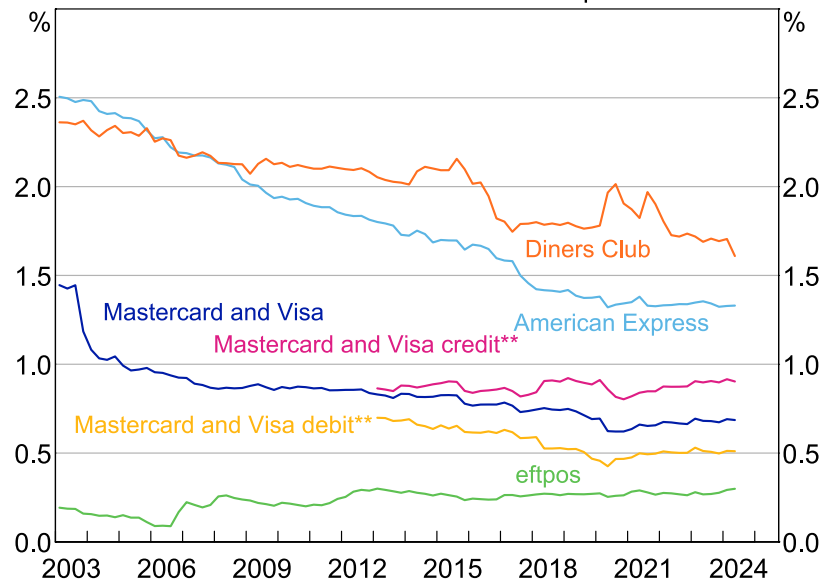
How do consumers respond to surcharges?

Many consumers dislike surcharges and some take steps to avoid paying them.³ In 2022, around 45 per cent of consumers said they would choose a non-surcharged method when faced with a surcharge, and 20 per cent said that they would avoid shopping at a merchant that levies a surcharge.⁴ However, 30 per cent of consumers said they would use their preferred payment method and pay the surcharge. This may reflect that some consumers are willing to pay for the convenience of using contactless payments and that less consumers are carrying a non-surcharged payment method such as cash.

What has been the impact of surcharging regulation in Australia?

The RBA first implemented surcharging regulation as part of a package of payments reforms in 2003. Card payments have grown strongly in Australia since then and data on merchant service fees indicate that the costs per transaction for merchants to accept card payments have declined. The RBA's view is that surcharging has helped to put downward pressure on merchant service fees, particularly for charge cards such as American Express, which are not subject to interchange regulation (Graph 1). Surcharging works to lower payment costs for three-party schemes, such as American Express, by giving merchants the option to directly pass on the cost to consumers. This incentivises these payment schemes to lower fees so that either merchants are less likely to surcharge or consumers will still choose their payment option.⁵ Comparatively, Australia's overall card payment costs are lower than those in the United States, yet remain higher than in European countries (Graph 2).

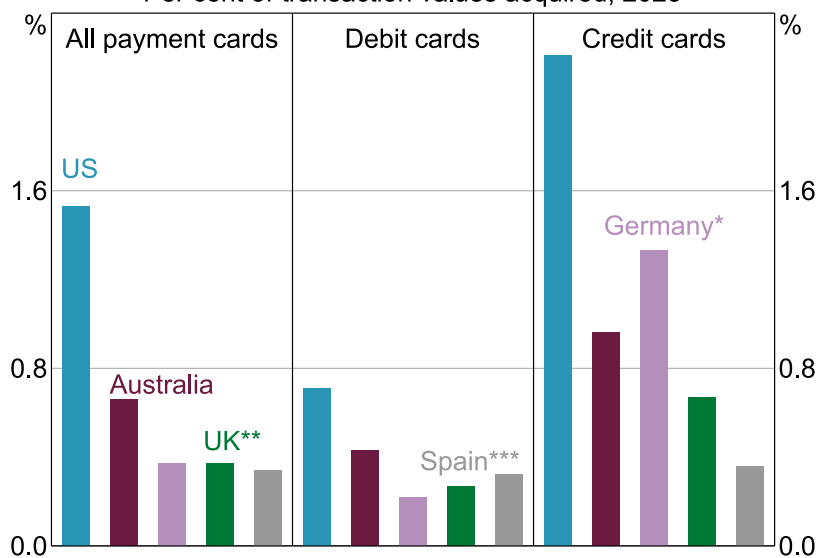
Graph 1
Total Merchant Fees*
 Per cent of transaction values acquired



* Series break in September 2020 due to change in reporting forms and in December 2022 due to change in collection coverage.
 ** Prior to changes in reporting methodology in June 2018, the average fee reported for Visa and Mastercard debit cards was slightly overstated and the average fee reported for Visa and Mastercard credit cards was slightly understated; the overall average fee for Visa and Mastercard was unaffected by the reporting change.

Source: RBA.

Graph 2
Merchant Service Fees
 Per cent of transaction values acquired, 2023



* 2017 data.
 ** 2022 data.
 *** Excludes three-party schemes.
 Sources: Banco de España; British Retail Consortium; Deutsche Bundesbank; Nilson Report; RBA.

Changes to the surcharging framework were implemented following the Review of Retail Payments Regulation in 2015–2016. The changes preserved the right of merchants to surcharge for more expensive payment methods but required surcharges in designated card systems to be more closely linked to the cost of acceptance.⁶ Changes to the *Competition and Consumer Act 2010* at the same time provided the ACCC with powers to investigate and take enforcement action when merchants surcharge excessively. These changes have helped reduce excessive surcharging, particularly in the airline industry, with companies adjusting their practices in response to the changes. Some enforcement action has also been taken against companies that engaged in excessive surcharging.⁷

What is the approach to surcharging in other jurisdictions?

Rules on payment surcharging vary significantly across jurisdictions. This section discusses the approach taken to surcharging in some other jurisdictions.

European Union, United Kingdom and Malaysia

Some jurisdictions do not allow surcharging of debit and credit card transactions. For example, the European Union bans surcharging on debit and credit card transactions, but cards issued by three-party schemes (such as American Express or Diners Club) and commercial cards are exempt because they are not covered by interchange fee regulation. Interchange fee regulation caps a portion of the main fees charged by payment service providers to merchants. European Union regulators argue that since these caps keep payment costs at a sufficiently low level, surcharging is not justified as it reduces price transparency and creates additional complexity for consumers. Malaysia also prohibits surcharging of debit or credit cards as part of its interchange regulation. The United Kingdom bans surcharging on all non-commercial debit and credit card transactions to prevent hidden costs for consumers.

United States and Canada

Most of the United States and Canada allow surcharging of credit cards, following lawsuits by merchants against credit card networks and card issuers in those jurisdictions. Credit card surcharges are subject to rules that limit surcharges to the cost of acceptance, up to a maximum allowable surcharge. A few states and provinces, however, have banned surcharging altogether. By contrast, the United States and Canada do not allow debit card surcharging because of ‘no-surcharge’ rules set by the card networks and, in the United States, interchange regulation.

New Zealand

New Zealand has allowed surcharging of credit and contactless debit card transactions since 2009, under agreements that the competition regulator entered with card schemes and banks. The competition regulator issued guidelines in 2023 that surcharges should not be greater than the cost of acceptance. The guidelines also indicate that there is no merchant service fee for the domestic eftpos scheme or where a debit card is inserted or swiped through the merchant’s terminal, so a surcharge should not be applied to these transactions.

Endnotes

- 1 Twelve payment systems are subject to the surcharging framework. The RBA has designated eight card schemes and they are covered by surcharging standards: Visa (credit, debit, prepaid), Mastercard (credit, debit, prepaid) and eftpos (debit, prepaid). The RBA also has undertakings from American Express, Diners Club and UnionPay that permit merchants to apply surcharges. PayPal revised its User Agreements in 2016 to allow merchants to surcharge PayPal transactions.
- 2 Tyro (2023), ‘Tyro Report: The Surcharging Landscape of Australian Businesses’, 13 June.
- 3 Choice (undated), ‘Credit Card Surcharging in Australia’, Report; McMullen S (2018), ‘Avoid Card Surcharges for Good with Fee-Free Shops’, Finder, 19 September.

- 4 Livermore T, J Mulqueoney, T Nguyen and B Watson (2023), 'The Evolution of Consumer Payments in Australia: Results from the 2022 Consumer Payments Survey', RBA Research Discussion Paper No 2023-08.
- 5 Three-party card schemes, like American Express, do not have interchange fees so they cannot be subject to the RBA's interchange regulation. Interchange fees are wholesale fees set by four-party card schemes such as Mastercard, Visa and eftpos that require payments from the merchant's payment service provider to the cardholder's issuer on every transaction. Three-party schemes do not have interchange fees because the merchant's payment service provider and the cardholder's issuer are the same institution: the operator of the three-party scheme.
- 6 RBA (undated), '2015–16 Review of Card Payments Regulation'.
- 7 ACCC (2019), 'Europcar to Pay \$350,000 Penalty for Excessive Card Payment Surcharges', Media Release No 146/19, 14 August; ACCC (2021), 'Nine Entertainment Pays Penalties for Alleged Excessive Payment Surcharges', Media Release No 100/21, 2 July.