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Dear Mr Connolly

Response to the Merchant Card Payment Costs and Surcharging Issues Paper

Thank you for the opportunity to respond to the Reserve Bank of Australia's (RBA) Merchant Card Payment Costs and Surcharging Issues Paper (Issues Paper).

About Co-operative Supermarkets Australia

Co-operative Supermarkets Australia (CSA), coopsupermarkets.com.au, is a not-for-profit membership organisation set up for independent Australian retailers. CSA was formed in 2019 and has attained ACCC approval to collectively negotiate on behalf of its retailer members.

The current membership represents over 560 retail outlets and includes members ranging from single store operators to large multi-store owners such as Ritchies, Drakes, Hill Street Grocer, Karellas Group and Bernardi's. Annual aggregated sales of the membership base are circa \$4 billion.

The supermarket and liquor retail segments, in which most of CSA's members operate, is a highly competitive low margin industry dominated by four main players: Woolworths, Coles, ALDI, and Metcash (IGA).

CSA's mission is to create a successful future for independent retailers by providing them the opportunity to have more independence and control (e.g. from Metcash) to deliver greater, sustainable, profitability. CSA has 40 direct product suppliers and "cost of doing business" providers covering areas such as merchant services, waste management, consumables and packaging that provide members with immediate savings by offering great deals across the membership base.

CSA has negotiated strategic merchant rate agreements with two card schemes and merchant services pricing incorporating least-cost routing with a preferred payment services provider (PSP). When first implemented in 2021, these arrangements resulted in average fee savings across the CSA membership base of over 25%.

CSA has visibility of the merchant services fee structures available historically and currently to its members in the market from a range of PSPs.

Under the current market landscape, to achieve further fee savings to maintain its competitive market position, CSA would need to negotiate lower strategic interchange fees with the card schemes and a lower PSP margin.

CSA Views on the Questions Raised in the Issues Paper

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?

There has been minimal or no change in the RBA's benchmarks on the weighted average interchange fees introduced in the early 2000's, currently:

- 0.50% of the transaction value for credit cards; and
- 8 cents per transaction for all debit and prepaid cards.

When the RBA's regulatory reforms were initially introduced, Australia had some of the lowest interchange fees globally. However, as noted in the Issues Paper, interchange fees in Australia are now higher than in some jurisdictions such as Europe despite the significant increase in the volume of card/electronic payments over the last two decades which should have led to a lowering of the per unit costs due to the economies of scale.

Prima facie, for a card scheme, issuer, acquirer, processor, PSP or merchant, there should be no difference in the cost of processing a standard credit card, premium credit card, debit card, or prepaid card transaction; and the processing cost should be the same regardless of the size of the merchant.

Issuer costs for interest free periods and loyalty programs should be borne by the issuer and not subsidised or paid by the acquirer or merchant via a higher interchange fee (as currently occurs with standard and premium credit cards).

There also appears to be no justification for setting interchange fees on an ad valorem basis versus a per transaction basis.

We note that while interchange fees for merchant payments flow from the acquirer to the issuer, in other real-time payment systems in Australia, the structure is very different:

- ATM system – Bilateral interchange fees prior to March 2009 flowed from the issuer to the acquirer. When the RBA introduced the ATM system regulatory reforms in March 2009 to enable direct charging by ATM deployers, bilateral interchange fees were set at zero. Where exceptions have been granted for multi-lateral fees in sub-network arrangements or one-way bilateral arrangements, interchange has flowed from the issuer to the acquirer.
- New Payments Platform – There are no interchange fees flowing in either direction between receiving and paying institutions.

We note that while innovation has occurred in payments over the last decade with respect to in-store and online payments, e.g. support for contactless payments, digital wallets, more sophisticated fraud prevention platforms, and tokenisation, the investment cost of this innovation has been incurred by both issuers, acquirers, processors, and merchants.

Hence, CSA's views are the following:

- In a mature payments market like Australia, there is no justification for interchange fees, and certainly not for the flow to be from the acquirer (with the merchant ultimately paying the cost) to the issuer.
- Should the RBA persist in permitting interchange fees to flow from the acquirer to the issuer, then CSA's views are:
 - There should be no difference in interchange fees between credit cards (standard or premium cards), debit cards, and prepaid cards.
 - Interchange fees should all be set on a per transaction basis at the same level regardless of card type.
 - There should be no differentiation between the interchange fees paid by different sized merchants.

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

CSA sees no reason why foreign card transactions should be exempt from interchange regulation in Australia.

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

As noted in our response to Q1, we believe interchange fees should be eliminated completely, or as a minimum, changed to a single per transaction fee that applies regardless of card type and merchant size. The cap for such an interchange fee should be limited to the core services required for transaction processing and netted between the issuer and acquirer costs, so that one party is not unfairly incurring the costs of both parties.

The categories and levels of strategic merchant rates available to larger merchants are published on the scheme websites. However, the qualification criteria to obtain these strategic merchant rates, e.g. the minimum transaction volume thresholds (value and number), and the fees that must be paid to the card schemes to access these rates, are not transparent. Instead, the strategic merchant rate agreements must be negotiated bilaterally between each individual merchant and the card scheme. Should the RBA persist in permitting interchange fees and differential interchange fees based on merchant size, then CSA's view is that the qualification criteria to obtain different levels of strategic merchant rates and all related benefits should be transparent and available on the card scheme websites.

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

Increasingly, acquirers and PSPs are offering merchants interchange++ pricing where they quote only the PSP margin and pass through interchange and scheme fee costs. However, a typical PSP response when asked for upfront disclosure of scheme fee costs is that "scheme fees are complex, dependent upon the card mix,

dependent upon the card value, and can change from month to month" (the latter being because some scheme fees are based in USD). Each PSP also applies scheme fees at a card type or transaction level in a different manner. Hence, scheme fees become an unknown pricing component when merchants are looking to move to interchange++ pricing and seeking to switch between PSPs.

CSA's view is that scheme fees should be transparent and published on the card scheme websites in the same manner as interchange fees are today. Please refer to our response to Q5 and Q6 on regulating scheme fees to reduce the complexity to make it easier for this disclosure to occur.

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

As noted in our response to Q4, scheme fees are opaque and those set by Visa and Mastercard are highly complex relative to the simplicity of the eftpos scheme fee structure.

CSA's view is that scheme fees should be simplified to a single AUD based transaction fee and separate ad valorem fee (if needed), for each card type (i.e. credit, debit, prepaid).

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

Our recommendation in response to Q5 is to simplify the structure of scheme fees. If this change is implemented, then scheme fees can easily be disclosed on the card scheme websites which will increase the competitive pressure on scheme fees.

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?

While not all merchants have enabled LCR for in-person card transactions, CSA's view is that LCR on in-person card transactions is widely available, and merchants can readily request their PSP enable LCR for card transactions.

However, CSA's view is that the lack of universal availability of LCR on mobile wallet transactions today (e.g. Apple Pay, Google Pay, Samsung Pay, etc) and the inability in most cases for the merchants to choose the routing needs to be addressed through regulatory intervention. When LCR becomes available on mobile wallet transactions, it should be the merchant's choice to request that LCR be immediately enabled on all wallet transactions (as for card transactions) and not dependent on consumer selection.

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?

Please refer to our responses to Q1-Q6 in relation to transparency and eliminating or simplifying interchange fees and simplifying scheme fees.

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?

Currently, if a merchant is on a blended rate or single rate plan, there is no information on the merchant statement on the breakdown by card type of interchange fees, scheme fees, and PSP margins. This makes it difficult for merchants to seek more competitive pricing from alternative PSPs or move to an interchange++ pricing structure with an alternative PSP should they wish to switch.

For those merchants on interchange+ or interchange++ pricing structures, how acquirers display this information on the merchant statements can vary significantly.

Like the cost of acceptance information currently summarised on merchant statements, CSA's view is that summary information on the merchant fees paid by card type split between interchange fees, scheme fees, and PSP margin should be disclosed on the monthly merchant statements regardless of the pricing structure type.

In many cases, PSPs only show 12 months cost of acceptance data on the June statement. CSA recommends that the cost of acceptance data and fee split mentioned above should be disclosed for both the current month and the last 12 months on the monthly statements.

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)?

Yes, CSA believes this would make it easier for merchants, particularly small businesses, to make pricing comparisons between different PSPs.

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

CSA believes that the changes that we have proposed in our responses to Q3, 4, 5, 6, 9, and 10, would result in greater competition between 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?

There needs to be greater enforcement of the current surcharging regulations to limit surcharging to the cost of acceptance and for upfront disclosure by the merchant of the surcharge rates so that consumers can make an informed decision on what card to use to minimise the potential surcharge.

In addition to the current fines that can be levied on merchants that do not comply, fines should also be placed on PSPs that do not educate or monitor compliance to the regulations by their merchants.

Implementing the recommendations we have proposed on interchange fees in our response to Q1 and Q2 would significantly reduce the level of surcharge fees which would address the current community concerns.

Our understanding is that the RBA permitted surcharging to help merchants to incentivise consumers to select the lowest cost payment method thereby improving the efficiency of the payments system. However, with single rate plans (for credit and debit), under the current interchange fee structure, surcharging provides no incentive for consumers to use the lowest cost payment method as consumers and merchants are then oblivious as to what that might be. Banning the ability to surcharge when a single rate plan is in place would encourage PSPs to provide pricing plans with differential pricing for credit and debit. This issue only arises due to the different interchange fee structures currently in place for credit and debit.

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

There is community and government pressure to ban surcharging on debit cards as fewer consumers today carry cash for payment. However, without the regulatory changes to interchange fees and scheme fees that we have recommended in our responses to Q1, 3, 4, and 5, which would significantly reduce merchant services fees, banning surcharging on debit cards would unfairly mean the cost burden for debit card acceptance falls entirely on the merchant.

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

We believe that should the RBA action the regulatory changes we have recommended in our responses to the earlier questions then no additional regulatory action should be required.

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?

Surcharging on Buy Now Pay Later (BNPL) transactions should be permitted once the RBA has the legislative authority over BNPL providers to ensure parity between different payment methods.

Summary

Thank you for the opportunity to respond to the RBA's Issues Paper.

We are supportive of regulatory changes that seek to reduce payment acceptance costs, increase transparency, reduce complexity, reduce the disparity between small and large businesses, and increase competition, all of which should lead to lower costs to consumers.

We look forward to discussing our response with the RBA.

Yours sincerely,

James Lane

James Lane
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Co-operative Supermarket Australia