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Merchant Card Payment Costs and Surcharging – Consultation Paper

Revolut Payments Australia Pty Limited ("Revolut Australia") welcomes the opportunity to comment on the Reserve Bank of Australia's Consultation paper. As a fast growing subsidiary of a significant international payments company, Revolut Australia is a direct stakeholder in the card payment ecosystem within Australia.

Part 1: Assessment and Recommendations:

We appreciate the opportunity to provide comments on the RBA's interim report and Preferred Package. Revolut operates as an issuer, acquirer and merchant and strongly supports the objective of boosting competition, efficiency and safety. We are concerned that the RBA's set of proposed interventions will not deliver on this objective. We have summarised our assessment in Part 1 of our response and have provided responses to the questions posed in the RBA's report in Part 2.

In principle, Revolut agrees that the removal of surcharging is a necessary and beneficial reform that would greatly improve transparency and efficiency for consumers and merchants through simplified compliance and enhancing merchant incentives. However, we remain deeply concerned by the RBA's proposed interventions on interchange regulations which are intricately linked to the surcharge changes. We believe that, in its current form, the "Preferred Package" would lead to unintended and negative impacts on competition, efficiency and safety. In particular, we believe the proposal for international interchange has not taken full consideration of costs and outcomes.

We encourage the RBA to consider the following points before publishing their final recommendations in order to avoid any unwanted consequences.

International and domestic issuers have cost bases that are not comparable and therefore the RBA should conduct a separate assessment to inform inter-regional interchange caps.

The RBA's consultation paper acknowledges issuer cost benchmarks are based on domestic costs only, with no recognition of higher international issuer risks or servicing costs. We believe that this is an oversight by the RBA as there are considerable differences which should be taken into account when setting interchange for international issuers.

Lowering interchange without addressing issuer costs (domestic and international) will lead to lower investment in solutions that (i) increase customer protection (reduce fraud) and (ii) support innovation in the local banking industry.

For context, since Revolut launched in Australia in July 2019 it has made significant investment into improving the customer protection and payments experience for our users globally. Some of the Fraud reduction investments since launch in 2019:

- Fraud Toolkit: a team of 11 people including: Data Science, Data Analysts, Engineers and Operations. They have built and continue to manage 2 Machine Learning (ML) models, a 3DS model and an Authorisation model.
- ML models prevent our customers from card fraud events by scanning all Revolut card payments to detect which ones we should be stopping, freezing the card and asking for the explicit customer feedback to unfreeze. The ML models have a significant impact on our issuer fraud rates. They are now the one of the lowest of any issuer globally at 0.8-1.0bps[1]. When comparing Australian card present fraud levels, the RBA quotes 4 bps domestically and 10 bps internationally.[2]
- Additionally, we have made improvements to our UX to promote features that improve customer safety. For example improvements in wallet tokenisation UX that have led to 72% of Revolut users tokenising their card to wallet which has 10x less fraud compared to traditional credentials.[3]

By capping interchange without addressing the cost base, the business case for innovation and competition for domestic and cross-border payments is significantly weakened. For example, the RBA could do more to address wallet related costs - such as Apple Pay fees - that international and domestic issuers must pay in order to use the Apple Pay service. In Australia, 70% of Revolut users access our services via an Apple iPhone with Apple Wallet functionality.[4]

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[1] Revolut card payment fraud data analysis
[2] RBA review of merchant payment costs & surcharging
[3] Revolut card tokenisation & fraud data analysis
[4] Revolut analysis of Australia user device data

Reducing interchange shrinks the revenue pool that supports the development and delivery of services, particularly those, like Revolut, that provide customers services with low or zero FX margins. This not only discourages global fintechs from entering the Australian market but also limits the ability of domestic players to build sustainable, competitive offerings that prioritise customer safety features and innovation. Specifically, this has a higher impact on the non-bank players who do not have a comparative diversified revenue income stream as incumbent banks (e.g. deposits and credit products). Revolut's pricing structure allows for customers to choose their benefit level dependent on their own financial circumstances and preference for rewards (such as insurance, memberships and travel perks) and a proportion of our customers pay a monthly subscription for these benefits. However, Revolut has built its business on its main product (Revolut Standard) being available to all, making affordable services easily accessible with no monthly account cost.

The RBA could follow other global regulators such as the EU Commission to address these costs. If the RBA reduces the cost of card acceptance for international transactions without addressing scheme, wallet, or acquirer fees, it entrenches the dominance of traditional card networks in cross-border commerce. This undermines future competition from open banking, account-to-account payments, and new fintech-led solutions — all of which rely on a level playing field to scale.

Lastly, we are concerned that the RBA's proposed interchange rates have not been backed by a proven methodology, particularly when considering that the rates proposed by the RBA are lower than rates published by other major payment markets UK and EEA where Merchant Indifference Test (MIT) were used to calculate interchange rates. MIT is not a narrow cost-recovery exercise, rather it incorporates the full set of benefits that merchants derive from card acceptance such as lower fraud rate, faster checkout times, improved sales conversion etc. By not taking these benefits into account there's a risk of an arbitrarily low level of interchange. For example on domestic debit interchange; the RBA is proposing 0.12% versus 0.2% in UK and EEA.[5]

Reducing interchange is not guaranteed to benefit merchants and customers and can lead to cost shifting to other areas i.e. the "waterbed effect"

Reducing cross border interchange will only likely benefit the larger merchants on IC++ arrangements with acquirers. For the majority of smaller merchants on blended pricing, they are unlikely to see any cost savings passed onto them through this action. This is something that has been noted as part of the UK PSR's review into card acquiring in the UK.[6]

Interchange cuts can trigger a "waterbed effect", where issuers and acquirers recover lost revenue by raising scheme fees, acquirer margins, or other charges, as seen after the US Durbin Amendment.[7] Banks in the US offset lower debit interchange by increasing account fees and reducing free services, meaning total costs to merchants or consumers may remain unchanged or even rise.

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[5] EU Interchange Fee Regulation (IFR) & UK PSR IFR Guidance
[6] PSR card acquiring review
[7] Federal Reserve Impact of Price Controls

In respect of international transactions even if merchants do realise cost savings by lower international interchange, these transactions are proportionally so small (3% of card transactions)[8], that the likelihood of merchants actually passing on such cost savings to Australian consumers is very low.

If these reductions in interchange are not effectively passed on to merchants, especially smaller ones on blended pricing plans, the benefits of removing surcharging will not be realised. Without a robust mechanism to guarantee a full pass-through of savings, merchants may simply absorb these costs or raise their base prices, offsetting any benefits for consumers.

The removal of surcharging and reduction of interchange must be accompanied by equivalent scrutiny of three-party card schemes (e.g. American Express).

The PSB has acknowledged that reducing interchange in four-party systems risks advantaging unregulated three-party networks, which can sustain higher cardholder rewards through higher merchant fees. Without this, there is a risk that the reforms could inadvertently favour these unregulated networks, which can offer higher rewards to cardholders by charging higher merchant fees. This would undermine the goal of competitive neutrality and could lead to a less efficient payments system overall. The PSB's acknowledgement of a potential path to bring these networks into the regulatory perimeter is a positive step that must be pursued.

Revolut's Recommendation:

Based on our concerns, we recommend the RBA reconsider its Preferred Package, taking following actions to ensure the reforms genuinely enhance competition, efficiency, and safety in the payments system:

1. **Re-evaluate the proposed international interchange caps.**
   We strongly urge the RBA to decouple the inter-regional interchange proposal from the domestic reforms and reconsider it entirely. We recommend a phased approach:
   - **Delay inter-regional interchange regulation.** The RBA should first implement the surcharge ban and observe its effects. This would allow the market to adjust and for the RBA to conduct a comprehensive, separate assessment of international issuer costs, risks, and benefits before imposing new caps.
   - **In the interim, maintain flexibility for merchants on higher-cost international transactions.** If the RBA does not implement proportionate and evidence-based caps on inter-regional interchange, merchants should retain the ability to recover these higher costs, including through targeted surcharges. Only once fair and proportionate caps are in place, then the removal of surcharge should be considered supporting a simpler, more consistent pricing environment for consumers.

[8] Visa data submitted to RBA in 2024

2. **Adopt a transparent, rule based methodology for international interchange - specifically, an cross border-specific issuer cost study and a Merchant Indifference Test (MIT) calibration**
   The current proposal blends a domestic Issuer Cost Study with EU/UK benchmarking and inferred foreign-issuer costs, which does not amount to a clear methodology for application to Australia. We recommend that the RBA:
   - **Conduct a dedicated issuer cost study for foreign-issued transactions**, rather than inferring from domestic issuer data, to capture cross border-specific processing, fraud and scheme-fee costs faced by issuers.
   - **Calibrate caps using the MIT,** linking interchange to merchants' avoided costs so that caps are proportionate to the value acceptance created on the merchant side. This approach underpinned the EEA's 0.2%/0.3% IFR caps and would enhance predictability, neutrality and long-run efficiency in Australia. In addition, this would leave more scope for the development and long term viability and sustainability of competitive payment methods to the international card schemes, including potentially home grown alternatives. It would be extremely difficult for a new payments entrant to compete with artificially lowered pricing.
   - **Every issuer is different** and will likely have different costs - a comprehensive study is essential to avoid unintended consequences.

3. **Explicitly address issuer costs when lowering interchange**
   - To foster a healthy and competitive payments ecosystem, the RBA must not only regulate interchange fees but also address the costs that issuers face
   - If the RBA proceeds with lowering interchange, it must take concurrent action to address the underlying costs borne by issuers, in recognition that not all issuers can offset lower revenue with other revenue sources. This includes a careful review of scheme fees and fees charged by digital wallet providers like Apple Pay, which represent a significant cost for both international and domestic issuers. Reducing interchange revenue without addressing these costs,will weaken the business case for new entrants and investment in customer protection and innovation.

4. **Accelerate the inclusion of all payment schemes and methods into the regulatory perimeter**
   - The RBA must expedite its efforts to bring three-party networks (e.g., American Express) and other emerging payment methods like Buy-Now-Pay-Later (BNPL) services under the same regulatory scrutiny as the designated four-party networks. The government's proposed reforms to the PSRA to include three-party networks are a positive step that must be actioned.
   - This is particularly an issue with large co-branded cards portfolios. Qantas points linked credit cards, represent a 35% market share[9] of credit cards. As the reduction of interchange revenue will lead to a likely reduction in points offerings by 4th party scheme participants it will entrench the dominance in

[9] [Qantas results FY24]

co-branded cards of unregulated 4th party schemes, such as American Express who can continue to allow surcharging and thereby offer higher point rewards.

5. **Implement a robust pass-through mechanism.**
   The success of the RBA's proposed package hinges on whether merchants and consumers actually benefit from the proposed reductions. To address the risk of the "waterbed" effect, we recommend:
   - **Mandate greater transpoptionarency from acquirers.** The RBA's proposals to require acquirers to publish average costs of acceptance and provide more detailed merchant statements are a good start. However, the RBA should go further by mandating that acquirers on "blended" plans provide a clear, standardised breakdown of how the reduction in wholesale costs (interchange and scheme fees) is reflected in their pricing.
   - **Close monitoring of pass-through.** While enforcement options would be limited without a regulatory cap on merchant fees, the RBA (in conjunction with the ACCC) should actively monitor whether reductions in wholesale costs are flowing through to merchants - particularly small and medium sized enterprises (SMEs). If monitoring shows that savings are not being passed on, the RBA should consider further policy options to strengthen the effectiveness of the reforms.

Part 2: Revolut response to RBA questions

Q1 - *Would removing surcharging on designated card networks best support the RBA's objectives to promote the public interest through improving competition, efficiency and safety in the payments system? In particular, the RBA welcomes feedback on whether there are additional public interest considerations that should be taken into account for each policy option.*

See Part 1

Q2 - *Do the proposed changes to interchange regulation promote the public interest by improving competition and efficiency in the payments system?*

See Part 1

Q3 - *Are there further considerations for smaller issuers that the RBA should take into account to enhance competition and efficiency in the payments system?*

We are concerned that the RBA's proposed interchange caps may not adequately account for the specific challenges faced by smaller issuers, potentially hindering competition and efficiency. Smaller issuers often rely heavily on interchange revenue to fund their operations, fraud protection and innovation. The proposed reductions, which are above average costs for the major banks, could significantly impact these smaller players who face materially higher costs. This could threaten their viability, reduce competition in the issuing market, and compromise their ability to invest in customer protection and new technologies.

We believe the proposed methodology for setting interchange fees is insufficient. Instead of the RBA's cost-based approach, which may not fully capture all of the dynamics in the market, we recommend using a Merchant Indifference Test (MIT) to determine the optimal interchange rate. This methodology would better balance the incentives of merchants, card issuers, and consumers by aligning interchange fees with the actual value provided to merchants. This would correct market failures, support competition among various payment methods, and encourage socially optimal use of card payments. Arbitrarily low caps, without a holistic view of the market, could disincentivise innovative players from entering the Australian market, limiting consumer choice and payments innovation.

In addition to reviewing the interchange caps for smaller issuers and adopting the MIT, we recommend the RBA implement the following to ensure the reforms deliver on their objectives:

- **Decouple international and domestic reforms**: We urge the RBA to separate the international interchange proposals from the domestic ones and reconsider them entirely. If this is not possible, we propose retaining surcharging for international transactions until a comprehensive, separate cost assessment can be completed.
- **Address all wholesale costs**: The RBA should broaden its focus beyond interchange to address other significant wholesale costs, such as scheme and mobile wallet fees.
- **Ensure a level playing field**: The regulatory framework must be applied consistently to all payment providers, including three-party schemes like American Express, to foster fair competition. The acknowledgment of a potential path to bring these networks into the regulatory perimeter is a positive step that must be pursued.

Q4 - Do the proposed changes to the net compensation provisions effectively achieve the RBA's objectives and promote the public interest? Will Australian issuers sponsored by overseas entities be able to comply with the changes?"

Revolut Australia supports the proposed amendments to the net compensation provisions. Ensuring that all Australian issuers, including those sponsored by overseas entities, are subject to consistent requirements is critical to upholding the integrity of the interchange framework.

Q5 - Does the proposal for card networks to publish aggregate wholesale fee data achieve the RBA's objectives of improving competition and efficiency among the card networks? Does the proposal adequately balance the information needs of the market with commercial concerns?

Revolut Australia supports the proposal for card networks to publish aggregate wholesale fee data as it aligns with the RBA's objectives of improving competition and efficiency. Publishing this data boosts transparency for payment service providers (PSPs) and merchants, enabling them to better understand their costs, negotiate deals, and optimise routing decisions. This increased transparency introduces competitive pricing pressure on schemes, which is crucial for reducing payment costs.

> *Q6 - Does the proposal for card networks to work with industry to reduce the complexity and improve the transparency of their scheme fee schedules enhance the competitiveness and efficiency of the card payments system?*

The proposal for card networks to simplify and increase the transparency of their scheme fee schedules would enhance the competitiveness and efficiency of the payments system. The current complexity hinders payment service providers (PSPs) and merchants from understanding these costs, which are often passed on to merchants. Simplifying these schedules would promote clarity, support more informed pricing decisions by PSPs thereby improving efficiency. This initiative proposed interchange reductions, as it would help to prevent card networks from circumventing new regulations by raising scheme fees and would subject them to greater scrutiny.

> *Q7 - Does the proposed expectation on scheme fees achieve the RBA's objectives of competition and efficiency in the payments system?*

The proposal for the RBA to set an expectation that card networks justify any scheme fee increases may partially achieve the RBA's objectives of competition and efficiency, but its effectiveness is uncertain. This approach aims to introduce greater accountability and deter unjustified cost inflation by requiring schemes to provide clear explanations for fee increases. While this could put some downward pressure on fees, it stops short of direct regulatory intervention. The RBA itself acknowledges that a cap on scheme fees may be necessary if fees continue to grow faster than transaction values. The efficacy of this "expectation-based" approach relies heavily on the industry's willingness to comply and the RBA's ability to monitor compliance, which may not be a strong enough deterrent to prevent cost-shifting or anti-competitive behaviour.

> *Q8 - Should the PSB consider further regulatory measures in relation to the level of scheme fees to promote competition and efficiency in the payments system?*

The RBA should consider further regulatory measures, such as a cap on scheme fees, if the proposed transparency measures do not sufficiently curb fee growth. The RBA's own analysis notes that scheme fees have risen over time, putting upward pressure on merchant payment costs. While the proposal to require justification for fee increases is a good first step, retaining the power to implement more direct regulation, such as a cap, is a prudent and necessary backup. This would ensure that the RBA can effectively address potential anti-competitive behaviour or excessive fee growth, particularly in less competitive markets like credit cards, and prevent schemes from circumventing interchange regulations by shifting costs to scheme fees. This aligns with the RBA's broader objective of promoting competition and efficiency.

Q9 - Does the proposed requirement for acquirers to publish their merchants' cost of acceptance enhance competition and efficiency by helping merchants search for a better plan?

The proposed requirement for acquirers to publish their merchants' average cost of acceptance (CoA) is a positive step that would enhance competition and efficiency in the payments system. By making this data publicly available, merchants—particularly small businesses—will gain greater price transparency, enabling them to compare their current rates with those paid by similar-sized merchants and different acquirers. This increased visibility gives merchants more power to negotiate with their existing provider or switch to a better-value plan. As argued in Part 1, this measure is crucial for empowering merchants and ensuring that cost reductions are passed through the system, thereby promoting competition and efficiency.

Q10 - Does the proposal to amend the cost of acceptance reporting on merchant statements to include a breakdown for domestic and international cards promote competition by helping merchants receive more information about the fees they pay?

The proposal to amend cost of acceptance (CoA) reporting on merchant statements to include a breakdown for domestic and international cards will promote competition. This greater transparency will provide merchants with more detailed information about the fees they pay, helping them to better understand their costs and compare pricing across providers. This is especially important given the significant cost difference between domestic and international card transactions. We believe this enhanced transparency will empower merchants to optimise their pricing plans and negotiate more effectively with acquirers. Furthermore, we oppose the proposed exemption for taxi fares, as there is no clear public interest case for it, and retaining the exemption would undermine the goal of promoting transparency and competition across all sectors of the economy.

Q11 - Are there any changes that should be made to the RBA's existing industry expectation on LCR implementation to improve competition and efficiency in the debit card market?

Revolut Australia believes there is no strong case for a formal regulatory mandate at this time. The RBA has decided to maintain the status quo, trusting that ongoing competitive pressure will continue to drive further uptake and innovation in routing capabilities. Revolut believes that this stance is prudent, allowing for market-led solutions to evolve without the imposition of potentially costly and complex regulatory requirements that might not be suitable for all merchants.

Q12 - Does the PSB's preferred package meet its objectives of competition, efficiency and safety in the payments system? Are there any variations to the package that the PSB should consider that would yield higher net public benefits? Is there any additional evidence that the RBA should consider before finalising its decision?"

We are concerned that the PSB's preferred package may not fully meet its objectives of competition, efficiency, and safety in the payments system. While we support the removal of surcharging, we believe the package's proposed interchange fee reductions are too focussed on direct costs and do not take into account holistic market considerations. We believe this will lead to significant negative consequences.

The package also fails to properly account for the different cost bases of international and domestic issuers. The draft standards for interchange fees on foreign-issued cards do not appear to be based on a thorough cost assessment, raising the risk of disincentivising investment in critical areas like fraud protection and innovation. We also think the proposals do not contain sufficient measures to ensure that the cost savings from lower interchange will be fully passed on to merchants, particularly small ones, which would undermine the benefits of removing surcharging.

The package also risks creating an uneven playing field by not applying the same regulation to three-party card schemes (e.g., American Express). This could inadvertently benefit these unregulated networks and lead to a less competitive and less efficient payments system overall.

To yield higher net public benefits, the PSB should consider several variations. First, it should decouple the international interchange reforms from the domestic ones until a more detailed cost review of international issuers can be conducted. Second, it should explore measures to address other issuer costs, such as scheme and mobile wallet fees. Lastly, the RBA should consider a methodology like the Merchant Indifference Test to set interchange, as this approach would better balance the interests of all stakeholders and ensure the reforms foster a truly competitive and innovative payments landscape.

Q13 - What is your feedback on the proposed implementation timeline for these reforms?

We believe the proposed implementation timeline is too ambitious and carries significant risks to the stability of the payments system. The RBA has suggested an effective date of 1 July 2026 for surcharging and interchange changes, with some transparency measures coming into effect sooner. A phased and delayed approach is necessary to avoid unforeseen problems and ensure a smooth transition for all stakeholders.

Concerns with the Proposed Timeline

- **Complex Interdependencies**: The proposed reforms are highly interconnected. Rushing the implementation of surcharging removal and new interchange caps to the same deadline could lead to market disruption if one component of the system is not ready. For example, if surcharging is removed before merchants can fully realise the benefits of lower interchange rates, they may be negatively impacted.
- **Insufficient Implementation Time**: A six-month window for implementing these sweeping changes is too short. As the consultation paper notes, some providers estimated a cost of up to A$10 million and up to 20 months to ensure compliance with a partial removal of surcharging, and while a full removal is less costly, it still requires significant changes. This timeline is even more compressed for the transparency measures, which are proposed to begin reporting for periods starting in January 2026, with the first publication date in July 2026.

- **Unaddressed Issues**: The timeline does not allow for a more detailed analysis of critical outstanding issues, such as the lack of a formal "pass-through" mechanism to ensure merchants and consumers benefit from lower interchange, the competitive impact on unregulated three-party schemes, or an MIT interchange analysis. A delayed timeline would allow the RBA to gather further evidence and consult on revised policies to address these gaps.

  Q14 - Do the draft standards in Appendix D achieve the intended policy objectives? Are there factors that have not been properly addressed or considered in the drafting of the proposed standards?

We are concerned that the draft standards in Appendix D, while well-intentioned, may not fully achieve the RBA's objectives of promoting competition, efficiency, and safety in the payments system. We believe the proposed interventions on interchange regulation, which are intricately linked to the removal of surcharging, could lead to unintended negative consequences.

Interchange Fee Regulation

The draft standards for interchange regulation raise several key issues. The proposed caps on international interchange fees do not seem to be based on a comprehensive cost assessment of international issuers, which have different and often higher costs related to fraud and servicing than their domestic counterparts. We are concerned that lowering interchange fees without a detailed analysis of all issuer costs, including scheme fees and mobile wallet fees (such as those from Apple Pay), could disincentivise essential investments in customer protection and innovation. Reducing interchange revenue shrinks the pool of funds that supports the development of cross-border services and safety features, potentially harming the entry of global fintechs and limiting the ability of domestic players to build competitive offerings. The RBA should not assume that non-bank participants have the ability to absorb the impact of reduced interchange through raising other revenue streams.

Market Competition and Merchant Benefits

The draft standards risk creating an uneven playing field. The proposed reduction in wholesale costs is not guaranteed to benefit smaller merchants, who are often on blended pricing plans and may not see the savings passed on by their acquirers. Without a robust mechanism to ensure the full pass-through of these savings, the benefits of removing surcharging may not be realised, and merchants may simply raise base prices to compensate. Furthermore, a lack of equivalent scrutiny on three-party card schemes (e.g., American Express) could inadvertently favour these unregulated networks, which can offer higher cardholder rewards by charging higher merchant fees, thereby undermining the goal of a competitively neutral and efficient payments system.

Conclusion

In their current form, the draft standards have not fully addressed these critical factors, which could lead to unwanted consequences for competition, innovation, and safety in the Australian payments market. We urge the RBA to reconsider these points before finalising its recommendations to avoid harming the long-term viability of issuers and ensuring that the reforms deliver genuine benefits to merchants and consumers

We would be happy to engage directly with the RBA on this topic (including providing any further data points where possible). If you require further information or clarification on any of our comments, please contact Scott Jamieson at scott.jamieson@revolut.com.

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