

Submission to the Reserve Bank of Australia

Designation of Visa Debit

2 April 2004

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TransAction Resources Pty Ltd

1. Executive Summary

The issuing, acquiring and marketing methods used by Visa International and its members, as these relate to the Visa Debit product, have been a source of concern for Australian merchants since this product's inception.

The decision by the RBA to designate Visa Debit is welcomed by the AMPF, as this process will now ensure public scrutiny of a number of practices that continue to impose greater costs and risks than necessary on both merchants and consumers.

This paper provides the views of the AMPF on the specific observations made by the RBA relating to Visa Debit, namely:

- that interchange fees charged between financial institutions for the processing of Visa Debit transactions are the same as for Visa Credit card transactions,
- that Visa Debit cards cannot be distinguished at the point of sale from Visa Credit cards,
- the 'honour all cards' rule enforced by Visa requires that merchants accepting Visa Credit cards must also accept Visa Debit cards; and
- that Visa Debit cards are still subject to a 'no surcharge' rule.

In addition, the paper will comment on a number of issues not specifically identified by the RBA but which the AMPF believes should be factored into both draft and final standards:

- the possible future introduction of other scheme debit products and the applicability of the proposed standards to such products,
- the need to stop the use of misleading advertising in the promotion of Visa Debit, and
- the desirability of transparent reporting of Visa Debit data to both merchants and to the RBA.

We look forward to the publication of draft standards by the RBA.

2. Introduction

This submission is in response to the Payments System Board of the Reserve Bank of Australia (RBA) designating the debit card scheme operated by Visa International (Visa Debit), as a payment system on February 23rd 2004. The Australian Merchant Payments Forum (AMPF) wishes to provide further input to the formulation of draft standards and access regime guidelines relating to Visa Debit.

Whilst this submission will specifically discuss draft standards that should be implemented as part of the Visa Debit designation process, such standards and their final iteration should be drafted in such a manner as to apply to all scheme debit cards operating in the Australian market, current or future.

The AMPF provided a detailed submission to the RBA in late January 2004 relating to scheme debit cards.¹ This paper builds upon that submission.

2.1 Background

The RBA and the Australian Competition and Consumer Commission (ACCC) have conducted a number of regulatory and other reviews into card activities over the past four years. The above reviews largely originated with a joint study by the ACCC and the RBA into credit cards, debit cards and ATMs in 2000². Whilst the "Joint Study" referred to debit card networks, there was no separate analysis of scheme debit systems as operated by Visa in Australia and by both Visa and MasterCard internationally.

The RBA then proceeded to designate Visa Credit cards (along with MasterCard and Bankcard credit card products) on April 11 2001, leaving aside Visa Debit, resulting in a set of final credit card standards progressively coming into force from 1 January 2003.

As part of the current Visa Debit designation process, the RBA made the following observations about the Visa debit card system as it currently operates in Australia:³

- the interchange fees charged between financial institutions for the processing of Visa Debit transactions are the same as for Visa Credit card transactions,
- Visa Debit cards cannot be distinguished at the point of sale from Visa Credit cards,
- the 'honour all cards' rule enforced by Visa requires that merchants accepting Visa Credit cards must also accept Visa Debit cards; and
- Visa Debit cards are subject to a "no surcharge" rule.

The RBA, after a period of public consultation, proposes to issue draft standards as part of the Visa Debit designation process (most likely by mid 2004), with final reforms announced and gazetted by the end of 2004.

¹ AMPF: *Submission to RBA re Scheme Debit Cards* - 27 January 2004.

² *Debit and Credit Card Schemes in Australia – A Study of Interchange Fees and Access*, Joint Report by the RBA and ACCC, October 2000.

³ RBA: Media Release 23 February 2004 – www.rba.gov.au.

2.2 Objectives

The objectives of this paper are to:

- provide the AMPF's views on the possible content of draft standards relating to the four observations by the RBA of the Visa Debit system (as noted above), and
- further, provide the RBA with the AMPF's views on possible draft standards relating to issues identified in the AMPF's January 2004 submission, but not contained in the RBA's observations.

3. Proposed Draft Standards

The intention of the AMPF is to provide an objective, background and recommended action for each of the observations made by the RBA in relation to Visa Debit. In addition, the AMPF will deal with issues not covered by the RBA's observations but which its' members feel require attention by the RBA. The approach is not couched in a legal framework, as final drafting of standards is a matter for the RBA.

3.1 Visa Debit Interchange

Objective

To align Visa Debit transaction interchange fees, with those applicable to domestic debit (EFTPOS) transactions.

Such an alignment would acknowledge that despite the different processing requirements of these two product types, they provide at the point of sale, access to the same cheque or savings account.

Background

Visa Debit cards can currently be processed in two ways at the point of sale with the processing method determining the interchange payable:

- if the customer presses the [SAV] or [CHQ] button on the card terminal at the point of sale, then the card is processed as a normal EFTPOS transaction, using the domestic bilateral EFTPOS links and EFTPOS interchange fees apply. The account/s being accessed are the cardholders normal savings or cheque accounts held with their financial institution, or
- if the customer presses the [CR] button, the transaction is processed via Visa's international processing system (VisaNet) and the Visa Credit ad valorem interchange fee applies. Selecting the [CR] function accesses the same savings and cheque accounts as above, albeit via a different route.

The large majority of Visa Debit transactions for purchases at the point of sale are processed via VisaNet and not via the EFTPOS network, as a result of cardholders being urged to select the [CR] function at the point of sale.

Visa Debit transactions can also be processed in "card not present - CNP" environments (i.e. via the Internet and telephone). When used in this manner, cardholders' savings and cheque accounts are still accessed albeit via a different route, and merchants are faced with repudiation risk. That is merchants bear the risk that a transaction will be disputed because the cardholder's identity has not been authenticated.

EFTPOS interchange should also be applicable in these CNP environments as there is no difference in risk borne by the issuer due to the absence of a payment guarantee and automatic charge back to the merchant in the event of a dispute. Transaction routing is the only point of differentiation.

Visa Debit transactions (except at the point of sale when the cardholder specifically selects their cheque or savings account) currently attract the Visa Credit card interchange fee for simply accessing savings or cheque accounts. Visa Debit issuers, as pointed out in our earlier paper to the RBA, actively promote the practice for point of sale transactions, because as issuers they are paid an ad-valorem interchange fee⁴. As is also discussed elsewhere in this paper, such cardholder encouragement is to the detriment of merchants, the community and is deceitful in its' application.

Visa Debit cards have historically had an interchange fee ranging from 0.8% to 1.2% for purchases in the domestic market, depending on the transaction type. This was reduced from 1 November 2003, in line with new credit card rates that have interchange levels ranging from 0.517% to 1.045%.⁵ Linking Visa Debit interchange to Visa Credit is in the AMPF's view unjustifiable and misleading given that this product is a debit card product.

Furthermore, scheme debit cards are used at the point of sale without PIN authorisation, providing a significant degree of exposure to the merchant and cardholder. The ability to use Visa Debit cards without a PIN at the point of sale is simply condoning "signature based debit". Signature based EFTPOS is a practice that is seen as unacceptable in the Australian market by all participants including issuers and acquirers, except as a backup in certain circumstances. Issuers and acquirers do not allow consumers and merchants access via ostensibly more secure means (e.g. the telephone), except in the case of Bpay. They are however quite willing to allow signature based debit via Visa to continue.

Non PIN authorised debit account access is significantly less secure and therefore more prone to fraud than PIN verified transactions. As a result scheme debit card transactions represent higher risks and costs to merchants and consumers. In addition such transactions are also more time consuming for the cardholder and the merchant. Overall, the lack of PIN authorisation for Visa Debit results in a less efficient payment system.

The distortion in the current interchange environment that applies to Visa Debit encourages the proliferation of non PIN authorised debit account access. Unless interchange arrangements for both Visa Debit and EFTPOS transactions are aligned, these costs will continue to rise and further reduce the efficiency of the Australian debit card market. In other words Visa Debit issuers should not be rewarded for increasing the risks and costs to Australian merchants and cardholders.

⁴ AMPF: *Submission to RBA re Scheme Debit Cards* - 27 January 2004 p. 14.

⁵ Source: Visa International (www.visa.com.au).

Recommended Actions

In order to ensure alignment of Visa Debit interchange with that applicable to domestic EFTPOS transactions, the draft standard relating to Visa Debit interchange should include the following:

- removal of the transaction pricing distinction at the point of sale, between selecting [CR], [SAV] or [CHQ] when a Visa Debit card is presented. Regardless of the account selected the transaction should be subject to the same fee regime as applies to EFTPOS transactions,
- alteration of interchange for Visa Debit transactions on the following basis:
 - for card present transactions, interchange levels should be identical to those applying to EFTPOS. As noted elsewhere in this paper, such transactions are no different to normal EFTPOS in that both access the same deposit accounts held by the cardholder,
 - for CNP environments (e.g. telephone and internet) interchange should again be identical to that applicable to EFTPOS transactions. In this situation, the issuer is not faced with any greater level of risk than in a card present situation. The risk in this case is borne by the merchant,

This approach would bring Visa Debit transactions into line with other debit card products operating in the Australian market.

As noted above and in the AMPF's earlier submission to the RBA ⁶, it is our view that interchange fees for scheme debit card transactions should be the same as for EFTPOS transactions.

3.2 Card Identification

Objective

To alter the current identification characteristics of Visa Debit cards, in order that they can be clearly distinguished from other Visa card products regardless of the usage channel (e.g. point of sale, internet, mail / telephone order, paper based).

Implementation of this objective is a pre-requisite to operation of the draft standards proposed below, relating to "Honour All Cards" and "Surcharging".

Background

Visa International and issuers of Visa Debit cards in Australia have intentionally blended the identity of the Visa Debit card product with Visa Credit cards. Visa and their issuer members have alleged that Visa Debit products are indistinguishable from Visa Credit cards in order to remove merchant and cardholder confusion at the point of sale. This justification is not accepted. Merchants and cardholders globally are quite able to distinguish the plethora of Visa (and other scheme) co-branded card products when presented at their points of sale, all of which carry a myriad of designs, with the common thread of the Visa logo.

⁶ AMPF: *Submission to RBA re Scheme Debit Cards* - 27 January 2004.

Certain Australian issuers of Visa Debit also claim that they are unable to distinguish between Visa Debit and Visa Credit cards, when processing these transactions through their systems, as the Visa Debit products do not carry separate BIN ⁷ details. According to Visa International, their credit and debit cards do carry separate BIN details. In fact, in a submission to the RBA by a number of major Visa issuers it is stated that:

“The BIN number provides a unique identification for the issuer and the transaction flows through a different processing stream during the clearing process when it is switched to the issuer. In this sense, Visa Debit transactions can be separately identified from credit card transactions.”⁸

As separate Visa Debit BINs already exist, issuers of these cards are easily able to both differentiate the cards involved and report on these accordingly.

The AMPF is of the view that the actions of Visa Debit issuers to date, are deliberately designed to:

- encourage cardholders to select [CR] at the point of sale, and
- mask the fact (as far as possible), that merchants are paying credit card ad-valorem merchant service fees for transactions that are simply accessing their customers' savings or cheque accounts. There are no physical or system identification issues that genuinely stop Visa Debit cards being identified.

Recommended Actions

To ensure that Visa Debit cards are able to be distinguished by issuers, acquirers, merchants and cardholders:

- visually from Visa Credit cards, and
- electronically, when being processed,

the draft standard relating to card identification must mandate that from the date of gazetting of the standard,

- issuers commence issuing replacement Visa Debit cards with clear branding and identification markings on the front of the card,
- issuers continue issuing cards with a unique Visa Debit BIN number range encoded on the magnetic stripe on the card,
- all Visa Debit BIN's be published and made available to merchants on request, and
- issuers have a period of 3 years to re-issue their total Visa Debit card base with cards carrying clear identification markings.

⁷ The Bank Identification Number (BIN) is a code assigned to a card which identifies the card type and the issuer. The BIN comprises the first 6 digits of the card number.

⁸ *Visa Debit – Australia, Discussion Paper*, Submission to RBA by St George Bank, Bendigo Bank, Australian Association of Permanent Building Societies (AAPBS) and Credit Union Services Corporation (Cuscal), September 2001, p.15.

3.3 Honour All Cards Rule (HACR)

Objective:

To develop a draft standard abolishing the HACR in so far as it applies to Visa Debit cards. This would provide merchants with the option of choosing to accept or not accept Visa Debit cards regardless of their acceptance of other Visa products.

Implementation of this proposed draft standard can only occur with simultaneous introduction of the proposed “card identification standard” as above.

Background

The HACR was originally introduced by the card schemes as a means to ensure that any merchant that agreed to accept, for example, Visa Credit cards would accept all Visa Credit cards irrespective of the country of issue or the issuing institution.

The concern is that the rule has been abused to mandate that merchants must accept a range of different card types (for example Visa Debit products), even if it is detrimental to their business. In the Visa Debit case, merchants are forced to accept debit card products at the point of sale that attract an ad-valorem interchange fee, while accepting EFTPOS products with identical functionality on a fixed fee basis.

It is believed the HACR is currently under review by the card schemes in Australia, at least partly as a flow-on from the Wal-Mart case in the USA, referred to in our earlier submission to the RBA ⁹. The Wal-Mart case highlighted the incremental costs faced by merchants when forced to accept scheme debit products under the HACR. The US courts found in favour of Wal-Mart with a multi-billion dollar settlement being reached as well as the revocation of HACR as it applies to scheme debit products.

Some Australian merchants are also examining the relative merits of pursuing a similar case in Australia.

Recommended Actions

In order to provide merchants with the option of accepting or not accepting Visa Debit card products, a draft standard be created which mandates:

- the modification of the Visa HACR allowing merchants to accept scheme credit cards or scheme debit or both, at the merchant’s choice,
- where a merchant chooses to accept Visa Debit and in conjunction with the Card Identification standard proposed above, that the merchant be provided with appropriate signage / decals to signify such acceptance at the point of sale. For example, use of the “Visa Debit” brand in the UK and the “Electron” brand in Asian markets provides such flexibility to merchants in those markets. There is no reason why such branding and flexibility could not be applied to the Australian market,
- that such modification be effective from the date of gazetting of the final standard.

⁹ AMPF: *Submission to RBA re Scheme Debit Cards* - 27 January 2004.

To assist in this process and as noted under Card Identification above, scheme debit cards should be visibly different from credit cards and merchants should be provided with the BIN details of these cards.

3.4 Surcharging

Objective:

To develop a draft standard mandating modification of Visa scheme rules, allowing for surcharging of Visa Debit transactions by merchants when accepting such cards via all channels.

Background

The no surcharge rule can technically still be applied by Visa to their debit card products. This is despite the RBA's gazetted credit card reform in late 2002 (and applying from 1 January 2003) allowing merchants to surcharge Visa, MasterCard and Bankcard credit card transactions¹⁰.

Leaving aside the fact that Visa Debit cards were not included in the earlier designation process, merchants would currently find it quite difficult if not impossible to implement a differential surcharge on Visa Debit products, as these are indistinguishable from Visa Credit card products. As noted in the Objective relating to the Card Identification draft standard above, this issue must be addressed in order for surcharging to be able to be implemented by merchants should they wish to do so.

Recommended Actions

Develop a draft standard allowing merchant surcharging on all Visa Debit products. Further it is necessary to ensure that:

- such a standard comes into force immediately on gazetting of the final standard, and
- in order to be effective, is introduced simultaneously with the Card Identification & Reporting draft standard proposed .

3.5 Access Regime

Objective:

To develop a draft standard which allows Visa Debit card products to be issued and / or acquired by Specialist Credit Card Institutions (SCCI's), as defined by the Australian Prudential Regulation Authority.¹¹ Further that the draft standard provides for participation eligibility, terms of participation and transparency in line with the RBA's Final Reforms and Regulation Impact Statement.¹²

¹⁰ Reform Of Credit Card Schemes In Australia – Final Reforms and Regulation Impact Statement Aug 2002 p. 46.

¹¹ *ibid.* p.68.

¹² *Ibid.* p.48.

Background

As part of the RBA's designation of the credit card schemes operated by Visa, MasterCard and Bankcard as payment systems in April 2001, regulations were put in place governing interchange fees, surcharging and access. The designation process did not however explicitly cover Visa Debit card products.

Visa Debit cards are therefore technically, not subject to the Access Regime reform as gazetted by the RBA.

Whilst the issue of Access relating to Visa Debit has not been identified by the RBA within the current designation, the AMPF believes that there needs to be similar access reform for Visa Debit products as has been previously mandated for Visa Credit products. Emerging SCCI's must also be able to acquire Visa Debit and provided they are able to achieve full ADI status, also be able to issue such products.

To summarise the key credit card Access Regime reforms ¹³:

- any entity which is an approved deposit taking institution (ADI) in Australia is eligible to apply to participate in any of the designated schemes,
- the designated schemes cannot discriminate between SCCI's and other ADI's when setting entry criteria,
- participation in the schemes can be on the basis of,
 - issuer only,
 - acquirer only, or
 - issuer and acquirer
- the schemes cannot penalise a participant for conducting either issuing or acquiring activities to a greater or lesser degree than the other, and
- the schemes cannot prevent any participant from being a self acquirer, provided that participant can meet the obligations of an acquirer.

Recommended Actions

Develop a draft standard on Visa Debit access, allowing SCCI's to acquire transactions in line with SCCI acquiring criteria already in place for credit cards. As Visa Debit is a standard debit product accessing savings and cheque accounts, issuing of such a product should require full ADI compliance as currently provided for by the Banking Act.

4. Other Issues

In the AMPF's earlier paper to the RBA on Scheme Debit Cards, a number of matters were raised which should be considered by the RBA when drafting standards relating to Visa Debit.

¹³ *ibid.* p.49.

4.1 Future Products

As noted earlier in this paper, the RBA should take into consideration the possibility that debit products may be introduced by MasterCard for example, which mirror the current operations of Visa Debit. While it is not possible to develop draft standards for hypothetical products, it may be useful for the RBA to make a general statement as part of its' draft standards, clearly signalling its views on this issue. This would most likely cause new products to be introduced in a more considered manner and without the necessity of further designations.

4.2 Misleading Advertising

The practices of current Visa Debit issuers, whereby cardholders are actively encouraged to select [CR] at the point of sale as opposed to [SAV] or [CHQ], warrant comment by the RBA.

Encouraging cardholders via advertising and other means, to select more expensive processing options is to the detriment of merchants and also the community. Whilst the draft standards as proposed by the AMPF above, would by definition remove this practice in relation to Visa Debit, the negative nature of such actions should be clearly pointed out by the RBA for future reference.

4.3 Reporting

Neither issuers nor acquirers currently provide separate reporting of Visa Debit transactions. Merchants are provided with a single volume and value for the totality of their Visa traffic, with this then being the basis for applying ad valorem merchant service fees. Visa Debit statistics are also not reported to the RBA, as far as the AMPF can determine. Statistical data relating to the Australian cards environment does not contain separate information on Visa Debit.

Such approaches serve to diminish transparency and do not allow merchants to calculate the cost of scheme debit acceptance. Without specific requests, the RBA also appears unable to determine the incremental cost to the community of such products.

The AMPF would recommend that:

- Visa Debit transaction data (volumes and values) be reported to merchants by their acquirers on the same basis as currently occurs for credit card and EFTPOS data,
- transaction data (volumes and values) as well as issuing volume data be reported to the RBA by issuers and acquirers for inclusion in monthly card statistics, for public use, and
- within a period of 90 days from gazetting of the final standard, issuers and acquirers ensure that their systems are separately reporting Visa Debit transactions on the above basis.

5. Next Steps

The AMPF understands the processes required as part of the designation process. In the RBA's structuring of draft standards the AMPF would be willing to provide any further input as may be required.

The AMPF, from discussions with the RBA, understands the Visa Debit designation timetable to be:

- initial submissions to the RBA by late March 2004,
- draft standards published by the RBA by mid June 2004,
- further consultation period to approximately September 2004, and
- final standards published and gazetted in the fourth quarter 2004.