

Review of Retail Payments Regulation

Consultation Paper

May 2021

Contents

1. Executive Summary	1
2. Introduction	6
3. Issues and Preliminary Assessment	8
Box A: Principles to address tying conduct	15
Box B: Principles for LCR in the device-not-present environment	18
Box C: Online LCR in practice	19
4. Summary and Next Steps	47
5. Consultation	50
Appendix A: Summary of Stakeholder Feedback	53
Appendix B: Draft Standards	59

© Reserve Bank of Australia 2021. All rights reserved. The contents of this publication shall not be reproduced, sold or distributed without the prior consent of the Reserve Bank of Australia.

ISBN 978-0-6489163-3-8 (Online)

1. Executive Summary

This paper presents the preliminary conclusions of the Payments System Board (the Board) following the public consultation process undertaken after the release of the *Review of Retail Payments Regulation – Issues Paper* (the Issues Paper) in November 2019. This paper also includes for consultation some draft standards that would implement the preliminary conclusions, consistent with the requirements of the *Payment Systems (Regulation) Act 1998* (PSRA). The Bank seeks comments on these preliminary conclusions and draft standards, with the expectation that the Board will reach its final conclusions in the second half of 2021.

A summary of the key preliminary conclusions is provided below. This paper should be read in conjunction with the Issues Paper, which includes discussion of the Bank’s earlier reforms and recent developments in retail payments in some detail.

1.1 Dual-network debit cards and least-cost routing

The majority of debit cards in Australia are dual-network debit cards (DNDCs), which allow domestic debit payments to be processed via either the domestic scheme (eftpos) or one of the international debit networks (Debit Mastercard or Visa Debit). Least-cost routing (LCR), also known as merchant-choice routing, is functionality that lets merchants process contactless (‘tap-and-go’) DNDC transactions through whichever network on the card costs them less to accept. This choice can help merchants reduce their payment costs and increase competitive pressure between the debit networks. Indeed, the average cost of accepting debit card transactions has fallen as LCR functionality has been gradually rolled out over the past few years. Given their potential benefits for competition and efficiency in the payments system, the Board has strongly supported the issuance of DNDCs and the provision of LCR functionality to merchants.

However, the Bank has observed a number of emerging threats to the viability of LCR. One threat is a growing number of small and medium-sized card issuers choosing to issue *single*-network debit cards (SNDCs) instead of DNDCs. SNDCs allow payments to be processed through only the one debit network on the card, which prevents LCR. Card issuers considering or choosing to issue SNDCs have pointed to the additional costs of issuing debit cards with two networks instead of one. However, some issuers may also be choosing SNDCs in response to financial incentives from the debit schemes, including higher interchange fees on SNDC transactions (interchange fees are the fees set by card schemes that are paid by the merchant’s acquirer to the card issuer on each transaction). The Board is concerned that a significant reduction in DNDC issuance would make LCR unattractive for many merchants. Over time, this would likely impose significant costs on the payments system and broader economy due to the loss of competitive tension between the debit schemes. The Board considers that policy action to limit, and slow, the shift to SNDCs is therefore desirable.

Some merchants have also alleged that the international schemes have been dis-incentivising the take-up of LCR by making low ‘strategic’ interchange rates on credit card transactions conditional on the value or volume of a merchant’s debit card transactions. While the Australian Competition and

Consumer Commission (ACCC) has carried out some investigations into such ‘tying conduct’, there is scope for the Bank to take additional action to prevent such anti-competitive behaviour.

More broadly, despite the benefits of LCR, take-up by merchants has remained low. The Board has therefore considered whether further policy action was warranted to promote the availability and take-up of LCR functionality for both ‘device-present’ (in-person) and ‘device-not-present’ (online) transactions.

Taking these factors and developments into account, the Bank is proposing the following policy framework for DNDCs and LCR:

1. **The Bank would state an explicit expectation that the major banks will continue to issue DNDCs, with both schemes to be provisioned in all relevant form factors offered by the issuer (such as in mobile wallets as well as physical cards).** The Board has weighed up the economy-wide benefits from greater DNDC issuance against the incremental costs to issuers of supporting a second debit network. On the basis of the evidence and feedback the Bank has received to date, the Board is not convinced that the benefits of extending any requirement to issue DNDCs beyond the major banks would outweigh the additional costs imposed on those smaller issuers, though it invites stakeholder views on an alternative option of mandating broader issuance of DNDCs.
2. **The Bank’s interchange standards would be amended to set a lower cents-based interchange cap for SNDC transactions than for DNDC transactions.** This would limit the possibility of schemes using interchange rates to incentivise SNDC issuance, which could accelerate the shift towards SNDCs. (Details of the proposed caps are provided in the following section.)
3. **The Bank would state an expectation that all acquirers and payment facilitators (which provide card acceptance services to merchants) will offer and promote LCR functionality to merchants in the device-present (in-person) environment.** The Board does not see a need for explicit regulatory requirements regarding the provision of LCR at this stage. This reflects the progress that has already been made by acquirers and payment facilitators on developing this functionality and the other policy actions being taken to address specific threats to the viability of LCR.
4. **The Bank would state an expectation that the industry will follow a set of principles regarding the implementation of LCR in the device-not-present (online) environment.** While the Board supports the provision of LCR online, it seems too early for formal intervention in the device-not-present context as eftpos’ online functionality is still being rolled out. However, the Board also has some concerns that online LCR could be hindered by some market participants taking restrictive approaches to its implementation. The Board has therefore set out some principles to ensure that the provision of LCR online appropriately balances the interests of merchants, consumers and the card schemes.
5. **The Bank would explicitly prohibit schemes from engaging in ‘tying conduct’ involving their debit and credit card products.** This would supplement the implied prohibitions in competition law, helping to ensure that the debit schemes compete solely on the basis of their debit card offerings, thereby supporting competition in the debit card market.

1.2 Interchange fees

Interchange fees are wholesale fees set by the card schemes that are paid by acquirers to card issuers on each card transaction. They are passed on to merchants and are a significant component of merchants’ cost of accepting card payments. Under the Bank’s interchange standards, card schemes

must comply with interchange fee benchmarks; specifically, the schemes' average interchange fees, weighted by the value or volume of transactions in each interchange category, are required to be below a benchmark of 0.50 per cent for credit cards, and 8 cents for debit and prepaid cards. The benchmarks are supplemented by caps on individual interchange rates, which limit the disparity between fees applicable to larger 'strategic' merchants and smaller businesses. These ceilings are currently: 0.80 per cent for credit cards; and 15 cents, or 0.20 per cent if the interchange fee is specified in percentage terms, for debit and prepaid cards.

The Board's long-held view is that interchange fees should generally be as low as possible, especially in mature payments systems. At present, however, the Board does not see a strong case for significant reforms to the interchange regulations. The current interchange settings have been in effect for only 4 years and appear to be working well. In particular, the Board does not currently see a strong public policy case for lowering the weighted-average benchmarks or the credit card cap.

However, the Bank has noted an increasing tendency for interchange fees on certain debit transactions at smaller merchants to be set at the cents-based cap. The Board is concerned that this can result in smaller merchants facing unreasonably high costs for some low-value transactions (for example, a 15 cent interchange fee on a \$15 transaction is equivalent to 1 per cent of the total value of the transaction). To address this concern without significantly changing the overall interchange framework, **the Board is proposing to reduce the cents-based debit interchange cap from 15 cents to 10 cents for DNDCs (and all prepaid cards) and 6 cents for SNDCs** (the rationale for different caps on DNDCs and SNDCs is explained in the section above). The schemes would still have considerable flexibility to set a range of interchange rates on different types of transactions, including by making greater use of percentage-based fees. Schemes would also have the ability to restructure their interchange schedules if they wished to minimise the impact of the lower cap on overall issuer revenues.

The Board also sees a case for increasing the transparency of interchange fees on domestic transactions on foreign-issued debit and credit cards. **The Board is proposing to require schemes to publish interchange fees on transactions on foreign-issued cards on their websites**, which would be a low-cost way of shining a light on these relatively high fees.

1.3 Scheme fees

Scheme fees are payable by both acquirers and issuers to the card schemes for the services they provide. They are an important component of the costs faced by merchants in accepting card payments (because they are passed on by acquirers), as well as the costs borne by issuers for providing card services to their customers. The Board has held concerns for some time about the opacity of scheme fee arrangements to end-users of the payments system, with some indications that this has allowed for scheme fees to increase over recent years. The opacity could also, in principle, make it easier for schemes to implement fees or rules that may be anti-competitive or have the effect of circumventing the Bank's interchange fee regulation.

Meaningful disclosure of scheme fees could partly address these concerns, thereby improving efficiency and promoting competition in the payments system. At the same time, the Board acknowledges that there is a degree of commercial sensitivity around scheme fees, and that disclosure requirements could increase the compliance burden for the industry. The Board considers that the following proposal strikes an appropriate balance between these considerations:

- **Schemes would be required to provide the Bank with access to their scheme fee schedules and all scheme rules, and to notify the Bank promptly of any changes to these.**
- **Schemes would also be required to provide quarterly data on scheme fee revenue and rebates to the Bank.** The Bank would consider publishing some of the aggregate data, to provide stakeholders with greater visibility over the average levels and growth rates of these fees across schemes. Larger issuers and acquirers would also be required to provide annual data on scheme fee payments to act as a cross-check on the data reported by the schemes.

1.4 Surcharging

The Board is not proposing to make changes to the surcharging rules introduced after the previous review of card payments regulation in 2015–16, because these rules are seen to be working well. **The Board is not proposing to require any ‘buy now, pay later’ (BNPL) providers to remove their no-surcharge rules at this time but considers that a policy case could emerge in the future and will keep this issue under review.**

The Bank’s surcharging rules give merchants the right to levy a fee on customers to recover the costs that merchants face in accepting payments using credit and debit cards. This is supported by rules that prevent merchants from surcharging excessively, which are enforced by the ACCC. Most merchants choose not to surcharge card payments, though having the ability to do so can help lower their payment costs and promote competition between card schemes.

A particular issue for this review is whether businesses that accept payments using BNPL services should be allowed to also apply a surcharge to recover the cost of accepting these transactions. BNPL transactions have been growing very strongly in recent years and these services have been adopted by a significant number of consumers and merchants, and are becoming more widely used for certain types of purchases. BNPL services are often free or inexpensive for consumers to use if payments are made on time, but tend to be expensive for merchants to accept. Despite this, providers of BNPL services typically have ‘no-surcharge rules’ that prevent merchants from passing on these costs to the consumers who benefit from using the BNPL service. The Board’s long-standing view is that the right of merchants to pass on costs to users of more expensive payment methods promotes competition and efficiency in the payments system. However, the Board also recognises that no-surcharge rules can sometimes help promote competition in the payments market by helping newer services build up their customer and merchant networks.

In considering this issue, the Board has sought to strike a balance between a regulatory environment that encourages innovation by supporting the ability of newer providers of payment services to compete with more established providers (such as card schemes) and providing newer players with an unfair competitive advantage in the medium term.

The Board has reached the view that there is not a clear public interest case for requiring any BNPL providers to remove their no-surcharge rules at this time. BNPL still accounts for a small share of payments in the economy when compared to some other electronic payment methods such as cards, despite recent strong growth. The Board is also conscious that the entry of newer players in the BNPL market has the potential to lead to lower merchant costs without the need for regulatory intervention. However, the arguments are finely balanced and a public policy case could emerge in the future if BNPL continues to grow strongly and becomes an even more prominent part of the retail payments landscape. The Board will therefore keep this policy issue under review in light of market developments.

1.5 Other Issues

The Consultation Paper also sets out the Board's preliminary conclusions on several other matters raised in the Issues Paper. These includes the following proposals:

- New initiatives to further improve the transparency of payment costs for merchants, to help reduce some impediments to competition in the acquiring market for smaller merchants.
- Some minor revisions to the net compensation provisions in the Bank's interchange standards, which include formalising recently issued guidance about when and how new issuers should begin certifying compliance with the provisions.
- Revoking the designation of the American Express Companion Card system, given that the four major banks have ceased offering companion cards.
- No regulatory action in the digital wallet market at this stage, but ongoing close monitoring of domestic and international developments. While the Bank's power to regulate in this area under current legislation is not entirely clear, this may be clarified following the Treasury's Review of the Australian Payments System (the Treasury Review).

2. Introduction

This paper is the second key document in the Bank’s review of retail payments regulation (the Review). It presents the Board’s preliminary conclusions on the matters discussed in the Issues Paper, reached following an extensive public consultation process. It also presents some draft variations to the Bank’s standards for card payment systems that would implement the preliminary conclusions. This chapter outlines the background and process for the Review, in the context of the Board’s mandate and competition and efficiency considerations.

The *Reserve Bank Act 1959* requires that the Bank’s payments system policy is to be directed towards controlling risk in the financial system, promoting the efficiency of the payments system and promoting competition in the market for payment services, consistent with the overall stability of the financial system. The Bank’s broad approach to payments system regulation has sought to encourage industry to undertake reform, using its powers only when a self- or co-regulatory solution has been unlikely to emerge to address public interest concerns. The Bank introduced a range of reforms to credit and debit card systems in the early 2000s. These reforms have subsequently been reviewed every five years or so to ensure that the Bank’s regulatory settings remain appropriate; the previous wide-ranging review took place over 2015–16.

Several developments informed the timing and direction of this Review. Two recent inquiries – one by the Productivity Commission, another by the Black Economy Taskforce – made some recommendations relevant to the Bank’s payments regulations. In addition, the retail payments landscape has changed appreciably in recent years, reflecting technological change, payments innovation, the entry of new providers and changing payment preferences of end users. Given this, it was timely to consider whether the current regulatory settings remained fit-for-purpose to achieve the Bank’s mandate.

At the same time, the growing complexity of the payments ecosystem and the emergence of new entities in the payments chain are raising a broader set of issues about the payments system. These relate to the implications of newer entities – like payment gateways, providers of mobile wallets and buy now, pay later (BNPL) services – on competition, efficiency and risk in the payments system, as well as the regulatory treatment of crypto-assets and so called ‘stable coins’. While the Bank has investigated some aspects of these issues in the Review, the broader question of whether the regulatory architecture remains appropriate for the changing payments system has been considered separately and concurrently in the Treasury’s Review of the Australian Payments System. This review is expected to report to the Treasurer shortly.

The Issues Paper sought the views of industry and other stakeholders and interested parties on a wide range of payments issues. While some of the issues were directly related to the Bank’s existing card payments regulation, the paper also asked whether there were any gaps in the payments system or regulatory issues that needed to be addressed outside the narrower topic of card payments. The Bank received over 50 written submissions in response to the Issues Paper, and consulted with a wide range of interested parties, including card schemes, consumer representatives, merchants, financial institutions and government. While the Bank originally expected to publish a follow-up paper in mid 2020, the Review was temporarily suspended in March 2020 in response to the COVID-19 pandemic.

In general, this paper is not proposing major reforms to the Bank's retail payments regulation. As noted in the Bank's submission to the Treasury Review, Australia's payments system is in most regards providing high-quality services for Australian households, businesses and government entities.¹ The Bank's past reforms to card payments regulation have contributed to this outcome, including the introduction of restrictions on interchange fees for debit and credit cards, and the removal of 'no-surcharge' rules imposed on merchants by some card schemes. Accordingly, the key policy changes proposed are relatively modest and relate mostly to: dual-network debit cards and least-cost routing; interchange fees; and the transparency of scheme fees. Extensive consideration has also been given to the no-surcharge rules imposed by some BNPL providers. For each of the key policy issues, this paper sets out a number of options, consistent with the Office of Best Practice Regulation's guidelines for regulatory impact analysis.

The paper is structured as follows: Chapter 3 briefly summarises the issues (with stakeholder views on these issues summarised in Appendix A), considers a range of options for each major issue and provides the Board's preliminary conclusions; Chapter 4 summarises the proposals and draft standards, and sets out the next steps; Chapter 5 invites submissions on this paper and the draft standards, which are set out in full in Appendix B.

1 See Reserve Bank of Australia (RBA) (2021b).

3. Issues and Preliminary Assessment

This chapter provides a brief summary of the main issues under review and sets out some options for reform, drawing on the material in the Issues Paper and the consultation undertaken to date. For the various options, relevant efficiency and competition considerations are discussed, along with potential costs and benefits, followed by the Board’s preliminary assessment. Several of the proposed reforms, particularly those relating to dual-network debit cards and least-cost routing, are inter-related and should be considered as a whole. Accordingly, in their feedback stakeholders should bear in mind that any shift away from the Board’s preferred option in one area may have implications for the Board’s preferred approach in another area.

3.1 Dual-network Debit Cards and Least-cost Routing

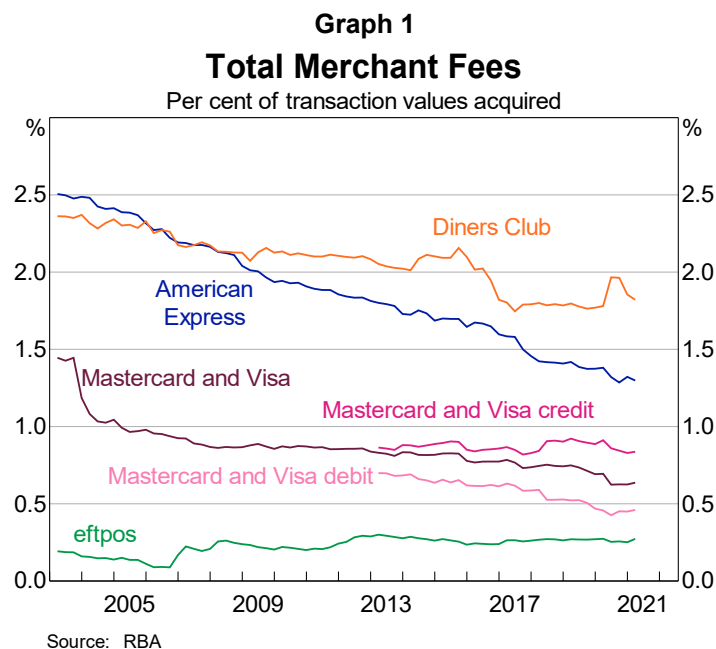
3.1.1 Summary of issues

Debit cards are now the most frequently used payment method in Australia. Over recent years, the Board has considered a number of issues relating to competition in the debit card market, most notably around dual-network debit cards (DNDCs). Around 90 per cent of debit cards issued in Australia are DNDCs, which allow domestic payments to be processed via either eftpos or one of the international debit schemes (Debit Mastercard or Visa Debit). For customers, DNDCs typically draw from the same deposit account and offer broadly similar protections to the cardholder in relation to fraudulent and disputed transactions regardless of which debit scheme processes the transaction. For many merchants, however, payments via eftpos can be significantly cheaper to accept than payments via the international schemes.

If a cardholder inserts their DNDC into a terminal to make a payment, they are able to select the debit card scheme to process the transaction. By contrast, if the cardholder makes a contactless (‘tap-and-go’) payment, the transaction is usually routed through the network that has been programmed as the default on the card (typically the international scheme). In recent years, however, financial institutions have begun providing merchants with ‘least-cost routing’ (LCR) or ‘merchant-choice routing’ functionality. LCR gives merchants the ability to route contactless DNDC transactions via whichever of the two networks on the card costs them less to accept. This can help merchants reduce their payment costs and increase competitive pressure between the debit schemes, incentivising the schemes to lower fees incurred by merchants. The Board has strongly supported the issuance of DNDCs and the provision of LCR because of this contribution to efficiency and competition in the payments system.

As LCR functionality has been gradually rolled out, schemes have responded to the increase in competitive pressure with lower interchange rates and scheme fees on routable transactions. The weighted-average interchange rates for Visa and Mastercard debit have declined and since late 2019 have been comfortably below the 8 cents benchmark. Industry participants have also reported that the international schemes have decreased scheme fees on some routable debit transactions by 40 per cent or more since mid 2019. This has translated into a reduction in the average cost of accepting debit card transactions through the international schemes over the past couple of years (Graph 1). At the same

time, however, there have been increases in interchange fees and scheme fees for some non-routable debit transactions, such as those made using mobile wallets, which are making up a growing share of total debit transactions.



Given the benefits to date from LCR, a key issue raised in the Issues Paper was whether policy action was warranted to promote the availability and wider take-up of this functionality. Following pressure from the Bank, most acquirers had implemented some form of LCR functionality by mid 2019. However, there remain some key differences in the LCR capabilities offered by different acquirers, with most not yet offering a version that maximises merchant savings by enabling ‘dynamic’ routing for each individual transaction. Furthermore, take-up among merchants remains relatively low. One major bank has automatically switched on LCR for eligible small merchants where it determined that they would benefit from the functionality. However, most other acquirers simply advertise the functionality to their customers, and the onus remains on merchants to understand the benefits of LCR and request it from their acquirer.

In addition, there are a number of emerging challenges to the viability of LCR. First, several smaller and mid-sized issuers have begun moving away from DNDCs towards single-network debit cards (SNDCs) which allow payments to be processed through only one (international) debit network. The switch to SNDCs reflects two factors. First, the international schemes have been keen to facilitate the issuance of these cards for some time and at least one scheme is offering higher interchange rates on transactions on SNDCs. In making the case for issuance of SNDCs, the international schemes have noted that some issuers still have single-network, eftpos-only ‘proprietary’ cards on issue, and LCR is not feasible on these cards. Second, issuers and international schemes have pointed in consultation to the additional cost of issuing debit cards with two networks instead of one. Given the largely overlapping functionality provided by the three debit schemes, smaller issuers in particular felt that supporting a second debit network yielded little benefit to their customers but generated significant costs, absorbing funds and resources that could be used elsewhere in their businesses. Some issuers have told the Bank that there are limited cost synergies in operating two debit networks. In particular, technical differences between the schemes were said to result in material duplication of issuers’ compliance and development costs. Differences in scheme rules and back-office processes also reportedly mean that supporting two

schemes increases the ongoing day-to-day costs of operating a debit card portfolio. Small and medium-sized issuers report that the additional cost burden of supporting a second debit network makes it harder to compete with the major banks, which can spread the costs of supporting two networks over a larger customer base. While estimates vary regarding issuers' costs of supporting two networks, these costs are likely to be more than a million dollars per year for mid-sized issuers. They are lower for smaller issuers which rely more on aggregators such as Cuscal, ASL and Indue, but they are still significant amounts in the context of the overall costs of running a debit card portfolio.

SNDCs reduce both customer and merchant choice, and so lessen competition between schemes at the point-of-sale. A particular concern is that a shift towards SNDC issuance could have the effect of making LCR unattractive for large merchants. When larger merchants adopt LCR and their DNDC transactions are routed via eftpos, they lose access to strategic interchange rates on other debit card transactions that continue to be processed through the international networks; the latter transactions would include transactions on DNDCs where the customer actively selects the international network or where routing is not possible because they are online or due to some problem with the chip or the issuer, as well as transactions on SNDCs. An increase in the prevalence of (international scheme) SNDCs would increase the pool of non-routable transactions that must be processed through the international schemes, while decreasing the pool of routable DNDC transactions. This would raise the cost of losing strategic interchange rates – lowering the savings from LCR – to the point where LCR might not be commercially attractive for large merchants. Stakeholders have suggested that with the ongoing shift towards mobile payments, which is separately increasing the pool of non-routable transactions processed through the international schemes (see below), the financial case for large merchants to adopt LCR is already becoming marginal.

In a world with more SNDCs, smaller merchants, which do not have access to strategic rates, might continue to benefit from LCR. However, if eftpos cannot compete for the volume of large merchants, its ability to compete for smaller merchants would also be weakened. In the extreme, as the lowest-cost network, its potential exit from the market would result in a significant lessening of competitive pressure in the debit market and would likely result in an increase in both interchange rates and scheme fees, impacting all merchants. This raises the question of whether policy action might be warranted to promote the ongoing issuance of DNDCs, so as to retain the competition and efficiency benefits that flow from them.

A second challenge to LCR is that technological changes have driven a significant shift away from the use of physical (plastic) cards at the point-of-sale to the use of new 'form factors', such as mobile wallets, through which LCR may not be possible. For mobile wallets, LCR is not possible, based on current implementation, because each network is separately provisioned and the wallet presents the credentials of only one network during payment; this network is typically the international debit network, which is set as the default, but it can be overridden by the cardholder. Nevertheless, DNDCs can still facilitate competition between schemes in the mobile context, as merchants can incentivise the customer to choose a particular network in their mobile wallet during the checkout process. However, not all mobile wallets and issuers currently support the provisioning of both networks of a DNDC; in some cases, only the international scheme is provisioned. This raises the question of whether the Bank should mandate the provisioning of both networks on a DNDC in all form factors, particularly mobile wallets.

Relatedly, eftpos has recently enabled its online payments functionality, which raises the possibility of LCR in the online (or 'device-not-present') environment. Indeed, the Bank is aware of several payments service providers already offering LCR online. The Board supports the provision of LCR online, given the

clear benefits that LCR has had in the card-present or ‘device-present’ environment, in terms of stronger competition and lower payment costs.² However, the online payment process is distinct from the device-present environment, which raises additional policy questions. A key issue is whether customers should be notified when merchants choose to route online transactions and whether customers should be given a choice to override merchants’ routing decisions. Some stakeholders are concerned about the comparability of the debit schemes’ online payment offerings, particularly in regard to security, and stress the importance of customer choice and notification. Indeed, one of the international schemes has already imposed rules relating to customer notification and choice. Other stakeholders are concerned about the frictions that these rules would introduce into the checkout process, in part due to customers’ poor understanding of payments, which could significantly deter the development and/or merchant take-up of LCR online. Accordingly, these stakeholders argue for greater merchant choice about how LCR operates in the online environment. In light of the possibility of scheme rules that could effectively discourage LCR, the Board has considered whether policy action might be required to support the provision of LCR online. The Board is also considering how the Bank might be informed in a more timely fashion of changes to scheme rules that have policy implications.

Another challenge to the viability of LCR is the potential for the international schemes to link strategic interchange rates on credit card transactions to the value or volume of merchants’ debit card transactions (or their decision to adopt LCR). Such ‘tying conduct’ penalises merchants that route debit card transactions to eftpos through higher interchange rates on their credit transactions, which could offset merchants’ savings from LCR. In effect, the international schemes could leverage their market power in the credit card market to dis-incentivise the take-up of LCR. In early 2018, the Bank sought and received assurances from the international schemes that they would not respond to LCR in ways that would limit the competitive pressure in the debit card market. Despite these assurances, several merchants have alleged that both Visa and Mastercard have engaged in such anti-competitive tying conduct, which the Board is particularly concerned about. The ACCC has investigated Visa’s conduct, due to its concerns that Visa may have limited competition by engaging in tying conduct, resulting in a court-enforceable undertaking from Visa in March 2021.³

3.1.2 Dual-network debit card issuance

Reform options

Given recent industry developments and the issues discussed above, the Board is considering three broad options in relation to the issuance of DNDCs, which represent an escalating degree of regulatory response:

Option 1: Maintain current arrangements

Issuers would continue to make the choice between issuing DNDCs and SNDCs based on commercial considerations. The Bank would continue to monitor market developments without any formal regulatory intervention.

Option 2: Explicit expectation of DNDC issuance for the major banks

The Bank would set an explicit expectation that the major banks would continue to issue DNDCs, with two card schemes to be provisioned in all form factors, including mobile wallets, offered by the issuer

2 From now on, this paper will use the terms device-present and device-not-present, rather than card-present and card-not-present, to acknowledge the growing tendency of card payments to move away from the traditional physical card form factor.

3 See ACCC (2021).

(where the functionality is supported by the scheme). There would be no presumption as to which two debit networks were included by issuers; various combinations of domestic and international schemes might be feasible. The Bank would also set a cents-based interchange cap that was lower for SNDC transactions than for DNDC transactions, which would lessen the incentive for SNDC issuance.

Option 3: Regulation mandating DNDC issuance for the major banks and medium-sized issuers

The Bank would require – through a change to Standard No. 2 of 2016 – that all issuers above a certain size threshold must issue only DNDCs, with two card schemes to be provisioned in all form factors, including mobile wallets, offered by the issuer (where the functionality is supported by the scheme). In designing the mandate, the Bank could draw on similar rules relating to dual-network debit cards in other jurisdictions, such as the United States.⁴ Under Option 3, there may not be a case for a lower cents-based interchange cap for SNDC transactions, depending on where the threshold were set.

Considerations

The Board acknowledges that, for any individual issuer, supporting two debit networks imposes additional costs that may not always be fully offset by the benefits for that issuer. However, as noted above, a widespread shift towards SNDCs could threaten the viability of LCR and the unravelling of LCR could impose significant efficiency costs on the system as a whole due to the loss of competitive tension between the debit schemes. Accordingly, maintaining the status quo (**Option 1**) is unlikely to best promote competition and efficiency in the payments system.

Instead, there may be scope for some policy action that recognises the system-wide benefits stemming from broad-based DNDC issuance. A significant intervention would involve the Bank imposing a formal regulatory requirement that all issuers above a certain size must issue only DNDCs. While the question of where to set the threshold would be a matter for judgement, the Board is interested in stakeholder views regarding a requirement that any authorised deposit-taking institution (ADI) accounting for more than 1 per cent of household deposits would be required to continue to issue DNDCs (**Option 3**); as of March 2021, this would have captured 10 ADIs out of a total of 94 retail-focused ADIs. It is noteworthy that some of the six non-major banks that would be captured by this threshold have already announced decisions to move towards issuance of SNDCs and so would be required to reverse these plans. This threshold would account for a large share of the debit market – around 88 per cent of household deposits in March – with the likelihood that in addition some smaller issuers would continue to issue DNDCs reflecting their own assessments of the costs and benefits of including two networks. This option would ensure that DNDCs continue to account for a large majority of all debit cards in the market, though it is possible that a threshold at the proposed level would see sufficient SNDC issuance that LCR would no longer be attractive for some merchants given the issues discussed above. A threshold set at a lower level and requiring significantly more ADIs to issue DNDCs might be required to provide greater assurance that LCR would remain viable for a wide range of merchants.⁵

4 The US Federal Reserve's Regulation II (Debit Card Interchange Fees and Routing) implements the so-called 'Durbin Amendment' to the Dodd-Frank Act. Among other things, it prohibits all issuers and networks from: restricting the number of networks over which electronic debit transactions may be processed to less than two unaffiliated networks; and inhibiting a merchant's ability to direct the routing of the electronic debit transaction over any network that the issuer has enabled to process them.

5 For example, a threshold set at 0.5 per cent of household deposits would capture a further 9 ADIs and bring total coverage to 94 per cent of household deposits. A threshold set at 0.1 per cent of household deposits would capture 38 ADIs in total and bring total coverage to 98 per cent of household deposits.

An intermediate alternative would be for the Bank to state an explicit expectation, rather than impose a formal regulatory requirement, that the major banks should continue issuing DNDCs (**Option 2**). This would be less interventionist, though formal regulation would be a possibility should the Bank's expectation not be met. Applying only to the major banks, it would capture around 74 per cent of household deposits. This would allow small and medium-sized issuers to avoid the cost of supporting two debit networks; though as noted above, not all non-major issuers would necessarily stop issuing DNDCs, especially as SNDCs might attract lower interchange on average under this option. With a lower proportion of DNDCs in the market, the commercial case for LCR would be weaker for merchants than under Option 3, though the threat of LCR would continue to exert some competitive pressure on interchange fees and scheme fees.

Preliminary assessment

The trend for some issuers to make the commercial decision to move from DNDCs to SNDCs is likely to continue in the absence of policy action. Over time, a continuation of this trend would likely impose significant costs on the payments system and broader economy, due to the loss of competitive tension between debit schemes to reduce costs to merchants. Accordingly, the Board does not support Option 1.

The Board has seriously considered the possibility of mandating the issuance of DNDCs by issuers over a certain size, and whether supporting DNDCs and LCR should be viewed as part of the social licence to operate for mid-sized banks. On balance, however, the Board is not convinced that the likely economy-wide benefits from a requirement on mid-sized (and possibly also smaller) issuers under Option 3 outweigh the clear costs that would be imposed on these issuers, including on their ability to compete with the major banks.⁶ Accordingly, on balance, the Board's preliminary assessment is that **Option 2** is the most appropriate course of action at this point in time. The Bank would set an explicit expectation that the major banks continue to issue DNDCs, with access to both networks in all relevant form factors, including mobile wallets, so that cards with dual-network functionality would continue to account for the majority of debit cards on issue. This 'expectations' approach, rather than formal regulation, is consistent with the Board's traditional presumption in favour of self-regulation to address policy concerns. The Bank's understanding is that the major banks intend to continue issuance of DNDCs, and that more generally they remain supportive of the domestic eftpos system.⁷ If this expectation was not met, the Board could consider imposing formal regulation in response. More broadly, if the cost of payments were to rise because LCR was no longer a viable option for many merchants and interchange fees or scheme fees were rising, the Board could consider if any other policy actions might be in the public interest.

In addition, the Board's view is that it is not appropriate for schemes to provide issuers with interchange-based incentives to issue SNDCs. Switching to SNDCs would reduce the cost burden faced

6 In the United States, the regulatory requirement to issue DNDCs applies to even the smallest financial institutions, though issuers with less than US\$10 billion in assets are exempt from the cap on interchange fees. The Board sees no case for such an exemption in Australia. Nevertheless, if stakeholders wish to make a case for Option 3, the Board would be interested in views as to possible policy measures (for example, somewhat higher interchange caps for small issuers) to offset the cost to small ADIs of supporting two networks.

7 The Bank notes that discussions about the possible consolidation of EPAL with BPAY and NPPA have been underway over the past year. In their recent application to the ACCC, the applicants (including the major banks, the two large retailers and a number of mid-sized entities) have committed to ongoing support for the roadmap for developing new functionality for the eftpos system. The Board has not viewed the consolidation discussions as material to the Review, except insofar that a consolidation could result in more streamlined decision-making by the three systems and their individual members which is likely to improve EPAL's ability to compete with the two large international debit schemes.

by an issuer, so there is little justification for schemes to provide higher interchange revenue at the same time. To limit the possibility of schemes using interchange rates in ways that would reduce competition and efficiency in the debit market, the Board's preliminary assessment is that the cents-based cap on interchange rates for SNDCs should be set at a lower level than that for DNDCs (the proposed levels of these caps are discussed in the 'Interchange Fees' section below).

3.1.3 Potential tying conduct by the international schemes

Reform options

The Board is considering two options to address the potential for international schemes to link strategic interchange rates on credit card transactions to merchants' value or volume of debit card transactions ('tying conduct').

Option 1: Leave the ACCC to investigate and take enforcement action against any anti-competitive tying conduct

Consistent with current practice, any alleged anti-competitive tying conduct would be investigated by the ACCC under the *Competition and Consumer Act 2010* (CCA).

Option 2: Explicitly address tying conduct

Under this option, the Bank would seek voluntary undertakings from the designated card schemes that they will not engage in tying conduct; if this was not feasible, it would introduce a new standard to explicitly prohibit such conduct by designated card schemes.

Considerations

The linking of strategic rates on credit card transactions to merchants' decisions on debit card routing would be contrary to the assurances that the schemes gave the Bank in early 2019 that they would not respond to LCR in ways that would limit competitive pressure in the debit card market. However, several merchants have alleged that both Visa and Mastercard have engaged in such tying conduct, which the Board finds particularly concerning. To date, the ACCC has investigated such alleged anti-competitive behaviour using its powers under the CCA. As noted above, the recent investigation by the ACCC has resulted in a court-enforceable undertaking from Visa that it would not engage in tying conduct. This is a positive outcome, which suggests that the Bank could continue to rely on the relevant provisions of the CCA and the ACCC's enforcement powers to address such conduct (**Option 1**).

However, there may be some merit in the Bank also obtaining specific undertakings from the international card schemes regarding tying conduct (or explicitly regulating tying conduct using its powers under the PSRA) (**Option 2**). Open-ended voluntary undertakings from both schemes regarding tying conduct (or an explicit prohibition in the Bank's standards) would provide certainty and can be expected to prevent such conduct taking place, rather than relying on regulators to take ex-post enforcement action to address such conduct. Compliance could be monitored through an annual certification requirement (and potentially enforced through the Bank's ability to issue directions under the PSRA).

Preliminary assessment

Given the potential negative impact of tying conduct on competition in the debit card market, the Board favours obtaining voluntary undertakings from the schemes that they will not engage in such conduct (or introducing a new standard to explicitly prohibit such behaviour) (**Option 2**). This would support

competition in the debit card market by helping to ensure that schemes compete solely on the basis of their debit card offerings. The Board is interested in stakeholder feedback on whether voluntary undertakings or a new standard would best achieve the intended policy outcome. The Board is also interested in stakeholder feedback on the principles outlined in Box A – which would underpin the provisions of any voluntary undertaking (or new standard) – and any practical issues with implementation.

Box A: Principles to address tying conduct

Principle 1: Merchants are able to make decisions with regard to the routing of DNDC transactions without implications for the interchange rates that are applied to their credit transactions.

1. If a merchant chooses to route DNDC transactions via a competing debit card network, schemes will not (for that reason, whether solely or in combination with other reasons):
 - (a) withdraw or deny access to, or increase, strategic credit interchange rates otherwise available to the merchant;
 - (b) withdraw or deny access to, or increase, the credit segment interchange rates applicable to that merchant; and/or
 - (c) otherwise increase the merchant's cost of accepting credit card payments.
2. Schemes will not make the offer of strategic credit interchange rates conditional on a merchant's debit volume/value or debit routing decisions.
3. Schemes will provide written reasons to a merchant for any withdrawal or denial of, or increase in, a merchant's strategic credit interchange rate.
4. Schemes will communicate to relevant merchants and acquirers that merchants' debit routing decisions and debit volumes/values will not influence their eligibility for strategic credit interchange rates.

Principle 2: Schemes will not incentivise merchants to route DNDC transactions through their network by leveraging credit during negotiations.

1. Schemes will not unreasonably delay the negotiation of strategic credit interchange rates with merchants. If a merchant requests to negotiate or seek certainty about applicable credit interchange rates prior to the negotiation of debit interchange rates, schemes will accommodate such a request.
2. Prior to commencing negotiations, schemes will provide merchants with clear criteria that apply for determining merchant eligibility for credit interchange rates (including strategic merchant rates and segment rates), including a clear statement that a merchant's volume/value of debit transactions and its debit routing decisions will not impact a merchant's eligibility for credit interchange rates.
3. When determining or applying merchant eligibility criteria for credit interchange rates (including strategic merchant rates and segment rates), schemes will not take into account a merchant's debit transaction volume/value or debit routing decisions. When determining the rate that applies to a category of merchants (including strategic merchants or segment merchants), schemes will not take into account the debit transaction volume/values or debit routing decisions of one or more of the merchants in the relevant category.

Schemes would be required to certify compliance annually.

3.1.4 Least-cost routing

Reform options

In relation to the provision of LCR functionality, the Board is considering three policy options:

Option 1: Maintain current arrangements

Under this option, the Bank would continue to monitor market developments in the provision of LCR across all relevant payment channels without any formal intervention.

Option 2: Explicit guidance on the provision of LCR by acquirers and payment facilitators

Under the second option, the Bank would state an explicit expectation that all acquirers and payment facilitators would offer and promote LCR functionality to merchants in the device-present environment; acquirers and payment facilitators would be expected to report to the Bank every 6 months on their LCR offerings and on merchant take-up. There would be no similar expectation regarding LCR in the online environment at this stage. However, the Board would set out a list of principles that it expects the industry to follow, to prevent the erection of barriers to the development and adoption of LCR online. If expectations for the provision of LCR are not met, the Board would consider formal regulation.

Option 3: Explicit regulation on the provision of LCR by acquirers and payment facilitators

Under Option 3, the Bank would require – through a change to the Bank’s standards – that relevant payments service providers offer or support LCR for both device-present and online DNDC payments. The Bank would also set explicit rules for LCR in the online environment to ensure that the interests of merchants and consumers are appropriately balanced.

For all 3 options, the Board is also considering whether the Bank’s information-gathering powers under section 26 of the PSRA should be used to require schemes to notify the Bank of all scheme rules and any changes to those rules (this would overlap with a similar proposal regarding scheme fee-related rules, discussed in the section on ‘Scheme fees’ below).

Considerations

The payments industry has made considerable progress in the provision of LCR in the device-present environment without any explicit regulatory requirements. However, as noted earlier, the take-up of LCR among merchants remains relatively low, and the functionality provided by many acquirers is still somewhat limited. Accordingly, policy action to promote the provision, and awareness, of LCR in the device-present context could lead to further cost savings for merchants and greater competitive tension between debit schemes. However, the benefits of policy action would need to be balanced against the costs acquirers may face in developing more sophisticated LCR functionality, particularly due to legacy information technology systems and increasingly complex scheme pricing models. Further, competitive dynamics in the acquiring market, including through new global and technology-focused providers, along with ongoing suasion from the official sector, may be sufficient to achieve the desired improvement in LCR functionality and awareness.

In the online environment, LCR is in its infancy, given that EPAL is still in the process of building out online capabilities for eftpos transactions. However, it is reasonable to expect that LCR could generate material competition and efficiency benefits in the online environment, just as it has done in the device-present environment. However, as noted earlier, LCR in the online payment context raises different policy considerations. In particular, the international schemes and some acquirers have argued that

material differences remain between the security capabilities and other product offerings of eftpos compared with the international schemes. Given the higher incidence of fraud in the e-commerce environment, these stakeholders have argued that LCR online could undermine security, adversely affecting all stakeholders in the online payments ecosystem.

Accordingly, the international schemes argued that cardholders should be notified of routing and given the option to override the merchant's choice. In the device-present environment, the Board (consistent with the views of most industry participants) determined that such notification was not required. This reflected a few factors: the debit schemes were judged to offer similar protections and functionality for customers; the physical space at the point-of-sale typically made it challenging to communicate information about LCR; notifying customers would have required the education of retail staff on the details of LCR; an override option would slow down the checkout process; and in the event that customers did have a preference for a particular scheme, they could insert their card in the payment terminal and make an explicit choice.

In the online environment it is arguably easier to give customers an explicit choice of scheme and also to notify them of LCR. However, it is important that LCR is implemented in a way that balances the interests of both consumers and merchants. For example, depending on how it is done, notification of customers or providing them with an option to override a merchant's routing decision could add significant friction to the checkout process. Many stakeholders, including merchant groups and some acquirers, have argued that this would lead to more transactions being abandoned, and would deter merchants from implementing LCR altogether. They have also argued that the majority of customers do not have a strong preference between debit card schemes and that there are not significant differences in the security capabilities of different schemes, so given that merchants incur the cost of processing a transaction and bear much of the fraud risk, they should be allowed to route transactions via their preferred network. Consumer groups were broadly comfortable with merchant routing without extensive notification, provided the consumer experience and protections were comparable across schemes.

As noted earlier, an international scheme has implemented a rule requiring acquirers and merchants to notify customers of LCR in the online context and to provide them with an override option. In line with the arguments above, many stakeholders have noted that they would not implement LCR online if they have to abide by such rules. Given the potential benefits of online LCR, and the likely barriers posed by such rules, there appears to be a strong case for the Board to at least set out its own views on how it expects LCR to operate online. This would help the industry coalesce around a model that, in the Board's view, appropriately balances the interests of merchants, consumers and the schemes.

The case of the United States, which is one of few jurisdictions globally where DNDCs and LCR (or merchant-choice routing) exist may be relevant here. In particular, while online merchant routing already occurs to a limited extent, the Federal Reserve has recently proposed some important clarifications to its regulation implementing the 'Durbin Amendment' to make it clear that issuers must ensure their cards enable online transactions by two unaffiliated networks. This is to ensure that there are no restrictions on merchants' ability to route in the online environment (and with no requirement of customer notification).

Preliminary assessment

The Board's preliminary view is that explicit regulatory requirements regarding the provision of LCR for device-present and online DNDC transactions (**Option 3**) is not necessary at this point in time. In the device-present environment, the industry has made considerable, albeit slow, progress on the provision

of LCR without explicit regulation, with all major acquirers now offering LCR in some form. In the online environment, eftpos' online capabilities, and so the potential for LCR, are still being developed. Accordingly, it seems too early to intervene with explicit regulation, given the Board's traditional presumption in favour of self-regulation. However, under the status quo (**Option 1**) there is some risk of the provision of online LCR being hindered by schemes or other market participants taking divergent, and in some cases restrictive, approaches to its implementation. So the Board will continue to use suasion and pressure on industry participants to ensure that the benefits of LCR are realised, and it sees merit in bolstering this by explicitly setting out its expectations for the provision of LCR (**Option 2**).

In the device-present environment, the Board's expectation would be that all acquirers should offer and promote LCR functionality to their merchant customers. Further action seems unnecessary given the progress that has been made to date, together with the fact that competition in the acquiring market should lead to further improvement in LCR functionality and awareness. In the online environment, the Board does not expect all acquirers and gateways to support LCR, at least not in the near term, partly due to stakeholders' concerns around security; the Board is comfortable relying on acquirers and gateways to choose whether to provide or support LCR functionality online based on their own assessment of the risks posed to themselves, cardholders and merchants. However, where LCR functionality is provided, the Board expects the industry to abide by the principles set out in Box B below (with Box C providing some stylised examples of how these principles might work in practice). In determining these principles, the Board has considered stakeholder feedback, and attempted to balance the interests of merchants, cardholders and schemes. The Board is persuaded that the majority of customers do not have a strong preference between debit card schemes. Further, given that merchants incur the cost of processing a transaction and bear much of the fraud risk, they should be able to route transactions via their preferred network, without significant friction being added to the checkout process. This outcome would be consistent with the approach being taken in the United States.

Finally, the rule implemented by one international scheme relating to online LCR has highlighted once again that scheme rules can have significant policy implications. Accordingly, the Board's view is that the Bank should be notified of all scheme rules and any changes to those rules. This could be achieved with minimal compliance burden for the schemes, as they would simply provide the same access to rules and notification of changes that is already provided to scheme participants.

Box B: Principles for LCR in the device-not-present environment

1. If a customer has been provided with the ability to choose their preferred debit network and they have made an explicit choice, this choice of network should not be overridden by the merchant or any other party in the transaction process. For example, this could include where the checkout page provided the explicit choice of debit network or where the customer used a digital wallet with a preselected debit network.
2. If a customer has not made an explicit choice of network and the transaction may be routed by the merchant or another party in the transaction process, there should be reasonable notification that routing could occur. In the case of new recurring transactions, it would be appropriate to notify customers only at the time of setting up the arrangement. In the case of existing recurring transactions, merchants should notify customers that their transactions may now be routed. The Bank does not propose to prescribe exactly how such notifications should occur.

3. If a merchant is using LCR, its website and checkout pages should not mislead customers about the choice of payment methods available, or the network that will process their debit transaction. In particular, the wording or visual cues presented when a customer pays with a debit card should not give the impression that a particular scheme will process the transaction if that is not the case; for example, if a checkout page shows a collection of scheme logos to signal how a customer initiates a card payment, the transaction should not be routed via a network that was not shown amongst the logos.
4. Card schemes should not impose rules or technical standards that have the effect of significantly reducing the likelihood of acquirers and gateways providing, and merchants choosing, LCR. For example, schemes should not have rules that:
 - (a) require merchants to give customers an explicit choice of debit network when first choosing their payment method (as this could preclude LCR)
 - (b) require merchants to notify customers about routing *in any specific way*
 - (c) require merchants to get customers' explicit consent to the merchant's routing choice, and/or to give customers the ability to override the merchant's routing choice (as this could introduce significant friction into the checkout process).

Box C: Online LCR in practice

This box steps through two stylised online transactions to clarify some aspects of how the principles outlined above might work in practice. These examples are illustrative only, and in practice merchants would be able to present debit payment options to their customers in many different ways while still adhering to the principles.

Consider a customer shopping online at two different merchant stores. Once the customer finishes adding items to their virtual carts, they proceed to the checkout pages and eventually reach the list of payment options. The customer prefers to use their (dual-network) debit card for online purchases.

At the first online store, the customer is presented with a 'debit card' option, which they select. The customer is then presented with the debit schemes accepted by the merchant, and is required to select their preferred debit network using a checkbox (as shown in the stylised example below). Once they select their preferred network, Scheme 2 in this example, they enter their card details and finalise the payment. The payment is then routed through Scheme 2, regardless of the merchant's own preference. This is because the customer's explicit choice of network cannot be subsequently overridden by the merchant, or any other party in the transaction process, and routed to another network (**Principle 1**).

PAYMENT	
<input type="radio"/>	REDEEM GIFT CARD OR REWARD POINTS
<input type="radio"/>	CREDIT CARD
<input checked="" type="radio"/>	DEBIT CARD
<input type="radio"/>	Network 1
<input checked="" type="radio"/>	Network 2
<input type="radio"/>	Network 3
Card number*	<input type="text"/>
Expiration date*	<input type="text"/> <input type="text"/>
CVV*	<input type="text"/>
<input type="radio"/>	PAYMENT OPTION 4
<input type="radio"/>	PAYMENT OPTION 5

At the second online store, the customer is presented with a 'debit or credit card' option, which they select (as shown in the example below). However, they are not asked to explicitly choose a debit network. In this case, the merchant would be free to route the transaction to their preferred network (one of the networks shown), but the customer should be notified that routing may occur (**Principle 2**). There are a number of ways in which customers could be notified of potential routing without disrupting the online shopping experience. Individual merchants could make their own decision about the most appropriate method of notification for their online store, including the location and the wording of the notice. The image below shows one stylised example (immediately below the scheme logos) of how a merchant could notify customers directly on a guest checkout page without interrupting the payment process. In this case, if the customer was not concerned about the merchant's routing decision, they would proceed to fill in their debit card details and finalise the payment. The merchant's payment service provider would then route the transaction through the merchant's preferred network.

PAYMENT	
<input type="radio"/>	REDEEM GIFT CARD OR REWARD POINTS
<input checked="" type="radio"/>	DEBIT OR CREDIT CARD
We accept	<input type="button" value="Network 1"/> <input type="button" value="Network 2"/> <input type="button" value="Network 3"/> <input type="button" value="Network 4"/> <input type="button" value="Network 5"/>
	<i>If using a debit card with two networks, your payment may be processed through either network.</i>
Card number*	<input type="text"/>
Expiration date*	<input type="text"/> <input type="text"/>
CVV*	<input type="text"/>
<input type="radio"/>	PAYMENT OPTION 4
<input type="radio"/>	PAYMENT OPTION 5
<input type="radio"/>	PAYMENT OPTION 6

Similar processes would apply if a customer was setting up a recurring payment or saving a DNDC on file with a merchant for future transactions – some merchants might give the customer an explicit choice of debit network for processing their future payments (in which case, the customer’s selection should not be subsequently overridden), while other merchants might choose not to do so (in which case, they should provide some notification to the customer if routing could occur).

If a customer already had a DNDC saved on file with a merchant or had an existing recurring transaction that used a DNDC (and had not explicitly selected a debit network), the merchant – upon adopting LCR – would similarly need to notify the customer if they planned to route any future payments; this could be done, for example, via an email or a notification when the customer next chose to use their saved payment method.⁸

Importantly, when customers were not given an explicit choice of network, the principles require that merchants must not mislead customers about which payment networks their transaction may be processed through (**Principle 3**). Using the second example above, in which the merchant displayed a selection of scheme logos, a DNDC transaction should only be processed through one of the networks displayed in that list.

3.2 Interchange Fees

3.2.1 Summary of issues

The first key issue relating to interchange fees is whether the levels of the card scheme interchange benchmarks and caps remain appropriate, particularly in light of the following:

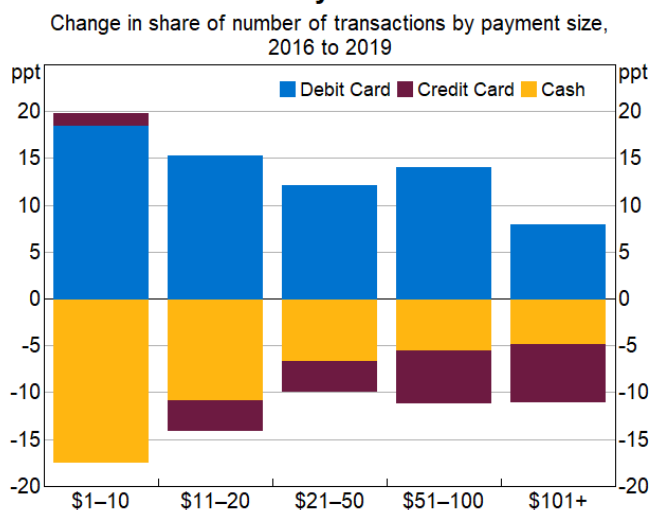
- recommendations by the Black Economy Taskforce (2017) and the Productivity Commission (2018) that interchange fees should be reduced or even eliminated, on the grounds that there is little justification for such fees in mature card systems such as Australia.
- the continuing decline in the average value of card transactions, particularly for debit cards. The average value of debit card transactions is now \$50, down from \$56 in 2016 when the Board lowered the weighted-average benchmark for debit and prepaid transactions from 12 cents to 8 cents. This trend is largely attributable to a migration of lower-value payments from cash to debit cards, amid the widespread adoption of contactless ‘tap-and-go’ technology (Graph 2). In 2019, 40 per cent of in-person payments of \$10 or less were made on debit cards, compared with 21 per cent in 2016.⁹ The share of debit card transactions has likely increased further since the emergence of COVID-19.
- the increased tendency for schemes to set debit interchange fees for non-routable transactions at smaller (non-strategic) merchants at the cents-based debit interchange cap of 15 cents (Table 1). The Bank’s regulatory framework, which is based around weighted-average benchmark, provides schemes with considerable flexibility in setting their interchange schedules, including to incentivise behaviours that support innovation and benefit the payments system. In the case of debit cards, the schemes have increasingly been using this flexibility to set low rates on some categories of transactions that are at risk of being routed to another scheme, while – to maintain interchange revenues for their issuers – increasing rates on other transactions that are less at risk

⁸ Routing for existing recurring transactions or for DNDCs saved on file may not be possible if the card details have been tokenised for only one of the schemes on the card. In this case, merchants that wish to route such transactions to a different network would need to ask customers to re-enter their card details to re-establish the relevant arrangements (with appropriate notification about possible routing occurring from that point).

⁹ See Caddy et al (2020) p18.

of being routed. The result has been increasingly complex interchange fee schedules, which offer lower rates for routable transactions at larger strategic merchants, accompanied by rates at the cap for many non-routable transactions (for example, card-not-present and tokenised card-present transactions) at smaller (non-strategic) merchants.

Graph 2
Consumer Payment Methods



Source: RBA calculations, based on data from Ipsos and Roy Morgan Research

The Board is concerned that setting rates at the cents-based cap results in unreasonably high costs for some low-value transactions at smaller merchants. For example, a 15 cent interchange fee on a \$15 transaction is equivalent to 1 per cent of the total value of the transaction. This is up to 15 times the interchange cost of the same transaction for larger strategic merchants. It is significantly higher than would apply based on the ad-valorem cap on debit transactions of 0.2 per cent, and higher than the interchange fee incurred if a credit card had been used (which is capped at 0.8 per cent).

A second key issue is whether the interchange regulations should be expanded to include transactions on foreign-issued cards, which attract interchange fees that are significantly higher than those on domestic cards. In 2019, the European Commission (EC) announced that it had accepted legally binding commitments from Mastercard and Visa to: reduce their inter-regional interchange fees to caps set by the EC; refrain from circumventing the caps; and publish inter-regional interchange fees.¹⁰ The Review presents an opportunity to consider whether a similar approach should be adopted in Australia.

A final key issue is the regulatory status of three-party schemes, which are currently not subject to the interchange standards, and can potentially incentivise greater issuance through higher cardholder rewards, funded by higher merchant fees. An issue for the Review is whether the Bank should regulate the merchant service fees charged by these schemes.

¹⁰ Inter-regional refers to transactions involving an entity from within the European Economic Area (EEA) and an entity from outside the EEA. The caps set by the EC were 1.50 per cent and 1.15 per cent for card-not-present credit and debit transactions respectively, and 0.3 per cent and 0.2 per cent for card-present credit and debit transactions (compared with caps of 0.3 per cent for credit and 0.2 per cent for debit on all intra-EEA transactions).

Table 1: Selected Debit Card Interchange Fees

Excluding GST; cents unless otherwise indicated; non-routable categories are in bold

Category	Mastercard		Visa		eftpos proprietary		eftpos dual-network	
	July 2017	March 2021	July 2017	March 2021	July 2017	March 2021	July 2017	March 2021
Strategic Merchant 1	2.82	1.0	2.0	1.0	0.0	1.5	0.0	1.0
Strategic Merchant 2	0.15%	2.0	5.0	1.5	1.8	3.0	1.8	2.0
Strategic Merchant 3		3.0	8.0	1.75	3.6	4.5	3.6	3.0
Strategic Merchant 4		4.0		2.0		6.0		4.0
Strategic Merchant 5		6.0		3.0				
Strategic Merchant 6		8.0		4.0				
Tokenised Contactless (>\$15)		15.0		15.0				
Consumer Standard: Card Present		4.0	8.0	4.0	13.6	11.0	4.5	4.0
Consumer Standard: Card Not Present/ Electronic/Digital	12.5	15.0	0.20%	0.20%	14.5	15.0	14.5	15.0
Consumer Premium: Card Present		15.0		15.0				
Consumer Premium: Card Not Present	0.20%	0.20%	0.20%	0.20%				

Sources: ePAL; Mastercard; Visa

3.2.2 Areas where reform is not proposed

The Board's preliminary view is that significant reforms to the interchange regulations are not necessary at present. In particular, the Board does not currently see a strong public policy case for lowering the weighted-average benchmarks or the credit card cap. It also does not see a strong case currently for expanding the scope of the regulations to capture three-party schemes.

The interchange benchmarks and credit cap

The current interchange settings have been in effect for only 4 years and appear to be working well. While the Board does not rule out lowering the weighted-average interchange benchmarks (8 cents for debit and prepaid transactions and 0.50 per cent for credit transactions) or the cap on credit card interchange rates (0.80 per cent) at some point in the future, on balance it does not consider such reform to be required at present.

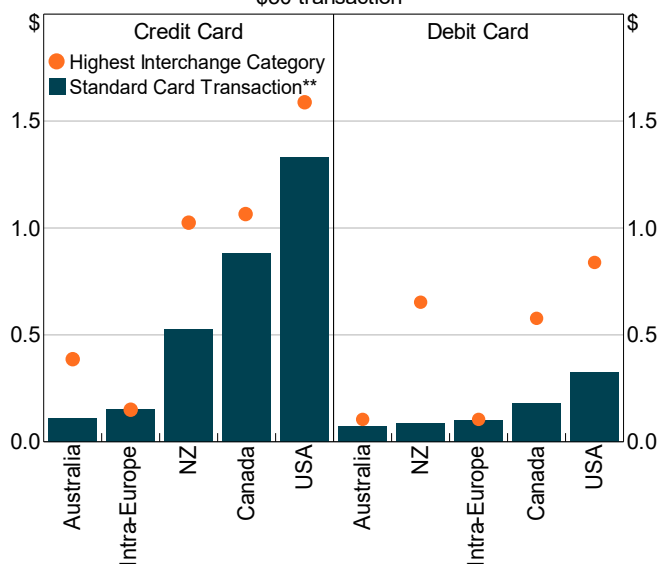
The Board's long-held view is that there is no strong justification for significant interchange fee payments in mature card systems. And it notes that there could be some benefits associated with lower interchange fees including, among other things: a reduction in payment costs in the economy; downward pressure on retail prices of goods and services for consumers; and lower barriers to entry for potential new methods of payment.

However, a range of indicators suggest that there is not a strong case for change to the benchmarks at present. There has been a significant decline in merchants' average cost of accepting card payments over the past two decades (see Graph 1 in the 'Dual-network Debit Cards and Least-cost Routing' section), to levels that are relatively low by international standards. Indeed, given that surcharging by

merchants is not widespread and that only a relatively small proportion of card payments incur a surcharge, it may be the case that card acceptance costs are now viewed as ‘sufficiently low’ by most merchants. Developments in the payments mix in recent years also suggest that current settings are contributing to positive outcomes, with a significant shift to debit cards from credit card payments (which have higher private and resource costs).¹¹ Further, Australian interchange rates for both debit and credit transactions are already low compared with most other economies (Graph 3).¹² One exception is the lower cap on credit card interchange fees in Europe (0.30 per cent, versus a weighted-average benchmark of 0.50 per cent and a cap of 0.80 per cent in Australia), but the Board considers it is too early to assess the European experience and draw implications for settings in Australia. Finally, in submissions to the Review, there was only limited support from stakeholders for reductions in the interchange benchmarks.

The Board notes that there would also be risks associated with further reductions in the weighted-average benchmarks. Lower interchange on debit transactions could make it harder for new debit issuers to enter the market and could disproportionately disadvantage smaller issuers, which may have fewer other sources of revenue to offset any interchange reduction. There is also a risk that a further reduction in the debit benchmark could incentivise issuers to promote greater issuance and use of (higher-cost) credit cards. In relation to the credit card benchmark, a further reduction could provide an advantage to both the three-party card schemes and other three-party open-loop systems such as BNPL arrangements. The benefits from lower interchange rates on credit card transactions could therefore be offset by a longer-term shift towards more costly three-party systems.

Graph 3
Four-party Scheme Interchange
\$50 transaction*



* Exchange rates as at 30 October 2020

** Refers to card-present transactions made on standard consumer cards

Sources: Mastercard; RBA; Visa

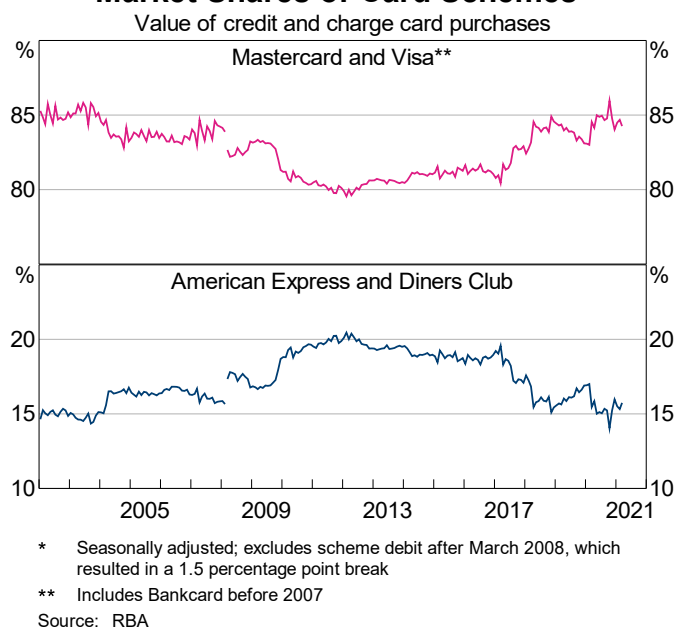
11 See Stewart et al (2014).

12 In May 2021, the New Zealand government announced that it will legislate to cap interchange fees for credit card transactions at 0.8 per cent and online debit card transactions at 0.6 per cent. Debit interchange fees are expected to remain at 0.2 per cent or less for card-present contactless transactions and 0 per cent where the card is swiped or inserted into the terminal.

Three-party schemes

The evidence does not suggest that three-party card schemes have benefited at the expense of the four-party schemes under the current regulatory settings. The market shares of three-party credit card schemes have declined markedly over the past few years (Graph 4). This was largely driven by the closure of the major banks' companion card programs following reforms introduced in the Bank's 2015–16 Review of Card Payments Regulation, which resulted in the American Express companion card system being regulated in a similar way to the traditional four-party schemes. The average cost of acceptance of three-party card payments has also declined since the previous review (see Graph 1 in the 'Dual-network Debit Cards and Least-cost Routing' section). These changes to merchant service fees charged by three-party schemes reflect the indirect competitive pressure flowing from interchange regulation on four-party schemes (including companion cards), as well as the continuing effectiveness of the ban on schemes imposing no-surcharge and no-steering rules.

Graph 4
Market Shares of Card Schemes*



3.2.3 Reform options

The Board's assessment is that policy responses may be warranted with respect to the high cost of some low-value debit (and prepaid) transactions that are subject to interchange rates at the 15 cents cap and transactions on foreign-issued cards.¹³

On the issue of the interchange cap, the Board has considered three broad policy options:

Option 1: Retain the current debit interchange caps

This option involves no change to the status quo, where schemes can set fees on debit interchange categories up to the current cap of 15 cents per transaction (or up to 0.20 per cent for interchange fees specified in percentage terms).

¹³ Unless indicated otherwise, for the remainder of section 2.2 'Interchange Fees', references to debit cards, transactions or interchange should be taken as referring also to prepaid cards, transactions or interchange.

Option 2: Reduce the cents-based debit interchange cap

This option involves reducing the cents-based cap for debit (and prepaid) cards. The particular proposal is to lower the cap to 10 cents for transactions on DNDCs (and all prepaid cards) and 6 cents for transactions on SNDCs (with the different cap for DNDCs and SNDCs consistent with the Board's preliminary assessment set out in the section above on 'Dual-network Debit Cards and Least-cost Routing'). The 6 cents cap would apply equally to SNDCs issued by the international schemes and to the remaining stock of proprietary, eftpos-only cards. There would be no change to the ad-valorem cap of 0.20 per cent for interchange fees specified in percentage terms.

Option 3: Require any debit interchange fees to be set in ad valorem terms

Under this option, the cents-based cap for debit (and prepaid) transactions would be eliminated, and the ad-valorem cap of 0.20 per cent would apply to all debit and prepaid interchange categories.¹⁴ The weighted-average benchmark would henceforth be set in ad-valorem terms. With an average debit card transaction value of \$50 in 2020, a weighted-average benchmark of around 0.16 per cent would be equivalent to the current cents-based benchmark of 8 cents.

The Board has also considered three possible responses to the high interchange fees on transactions on foreign-issued cards:

Option 1: No regulation of foreign-issued cards

This option retains the status quo, where foreign-issued cards are outside the scope of the interchange standards.

Option 2: Extend interchange regulation to foreign-issued cards

Under this option, there would be caps on interchange fees on transactions on foreign-issued cards. The interchange standards would be amended to make transactions on foreign cards subject to the same caps as apply to transactions on domestic cards, though they would not be included in the calculations for the observance of the weighted-average benchmarks. The schemes would be required to publish interchange rates for transactions on foreign cards on their websites.

Option 3: Publication of interchange fees on foreign-issued cards, but no regulation regarding fee levels

Under this option, the interchange standards would be amended to require schemes to publish the interchange fees on foreign cards on their websites. However, the fees on foreign cards would not be subject to the interchange caps or benchmarks.

3.2.4 Considerations

Debit interchange cap

The interchange caps have only been in place for 4 years, and leaving the debit (and prepaid) cap unchanged (**Option 1**) would provide the industry with stability in the regulatory framework. The current caps also provide the schemes with considerable flexibility to set a range of rates on different

¹⁴ The Board would also consider the case for setting different ad valorem caps for DNDCs and SNDCs, to lessen the incentive for SNDC issuance, in line with its preliminary assessment set out in the section above on 'Dual-network Debit Cards and Least-cost Routing'.

types of transactions to incentivise certain issuer and acquirer behaviours that benefit the entire network (for example, the adoption of new security features such as tokenisation).

However, in practice, the three debit schemes appear to have used the ability to set some interchange rates at the 15 cents or 0.20 per cent caps not only for the purpose of incentivising innovation or other actions that improve the payments system, but also for the purpose of holding up overall interchange revenues for their issuers by taking advantage of transactions that are not at risk of routing to another scheme. The Board is concerned that these actions are particularly disadvantageous for smaller merchants which do not benefit from strategic rates and that they can result in unreasonably high payment costs for some low-value debit transactions. While merchants have the option of recovering higher payment costs by surcharging debit transactions, in practice this may not be feasible due to the risk of customers abandoning the transaction and merchants may find it difficult to impose differential surcharges based on transaction value. Routine surcharging of debit transactions would also not be a desirable outcome, given that debit cards are now the most prevalent payment method for retail goods and services, and are increasingly replacing cash for low-value transactions.

Reducing the cents-based cap, to 10 cents for DNDCs (and all prepaid cards) and 6 cents for SNDCs (**Option 2**), would go some way to addressing the Board's concerns about the cost of payments for some low-value transactions, particularly at smaller merchants, without significantly changing the structure of the overall interchange framework. It would also reduce the disparity between the cost to small and large merchants for accepting similar transactions.

One concern raised by schemes and some issuers is that decreasing the permissible range of interchange fees would reduce the scope for using differential fees to incentivise behaviour, including behaviour that benefits the system as whole (such as implementing new security features). However, the Bank considers that the proposed lower cents-based caps would still provide considerable scope for differential pricing. Further, the range of fees that could be set in ad-valorem terms would be unaffected, with no change to the ad-valorem cap of 0.20 per cent.

Stakeholders have also suggested that lowering the cents-based cap would reduce the total interchange revenues flowing to issuers, particularly disadvantaging smaller issuers that are more dependent on these revenues. The Bank notes that a reduction in the cap would affect each scheme (and its issuers) differently, depending on the current structure of its interchange schedule and average transaction sizes. However, the Bank is not proposing to change the benchmark, which means that overall issuer revenue will not necessarily be impacted and the schemes would retain significant flexibility in their fee schedules, including the ability to make greater use of the 0.20 per cent ad-valorem cap.

Indeed, some stakeholders have proposed that schemes should be required to set all debit interchange fees on an ad-valorem basis (**Option 3**). While this would ensure that low-value transactions are not subject to disproportionate fees, the Bank notes that it would be a significant change to the interchange framework. A key rationale for the original cents-based benchmark and cap was that most of the costs of processing debit card transactions were unrelated to transaction value. For example, the messaging cost of a \$1 payment is no different to that of a \$100 payment, and debit transactions are not subject to many of the ad valorem costs associated with credit cards; they do not provide interest-free periods and typically do not offer rewards programs. While the Bank generally expects there will be some correlation between payment cost and transaction size, the original rationale for the cents-based nature of the benchmark remains relevant. In addition, as noted above, lowering the cents-based cap will likely result in more fees being set in ad-valorem terms, but without significantly changing the regulatory framework.

Foreign-issued cards

While the share of total card payments in Australia made using (more expensive) foreign-issued cards has grown over the past decade, it remains low - at 3 per cent in 2019 prior to a significant fall in 2020 due to the reduction in international travel in the pandemic. The impact of foreign-issued cards on system-wide payment costs, therefore, does not appear to be significant. There has also been no evidence of issuers attempting to circumvent the Australian interchange regime through offshore card issuance (which has been noted previously as a potential concern).

Nevertheless, given the higher cost of foreign card transactions, it may be desirable to increase the transparency of the interchange fees that apply to foreign-issued cards (**Option 3**). Greater transparency across schemes of the cost of accepting payments on foreign cards should bring greater competitive pressure on these fees.

3.2.5 Preliminary assessment

The Board's preliminary assessment is that the high cost of some low-value debit transactions, particularly for smaller merchants, is likely to persist under the status quo (**Option 1**). However, the Board is wary of making significant changes to the interchange framework, such as requiring schemes to set all debit interchange fees on an ad-valorem basis (**Option 3**), due to the potential for unintended consequences. Accordingly, the Board favours a reduction in the debit card interchange cap (**Option 2**) that would reduce the possibility of very high effective interchange rates on low-value transactions at smaller (non-strategic) merchants. This would not significantly change the overall interchange framework, which would still provide schemes with the flexibility to set higher interchange rates on some types of transactions to incentivise certain behaviours, and schemes would have the ability to restructure their interchange schedules if they wished to minimise the impact of the lower cap on aggregate issuer revenues. The Board is seeking feedback on the proposed caps of 10 cents for DNDCs (and all prepaid cards) and 6 cents for SNDCs.¹⁵

Given the higher cost of foreign-issued cards, the Board's preliminary view is that there is a case for increasing the transparency of interchange fees on such cards by requiring schemes to publish these on their websites (**Option 3**), rather than persisting with the status quo (**Option 1**). However, given the limited impact on system-wide costs and the absence of evidence that issuers are circumventing the domestic benchmarks through encouraging offshore issuance, broader regulation of these interchange fees (**Option 2**) does not seem warranted at this stage.

3.3 Scheme Fees

3.3.1 Summary of issues

The Issues Paper noted that there is very little transparency around scheme fees. Scheme fees are payable by both acquirers and issuers to the card schemes for the services they provide, mostly on a per-transaction basis. They are an important component of the costs faced by merchants in accepting card payments, as well as the costs borne by issuers for providing card services to their customers. A number of stakeholders have commented to the Bank that scheme fees have been growing over recent

¹⁵ As noted earlier, if the Board were persuaded to mandate that all issuers above a certain size threshold must issue only DNDCs (Option 3 in the section on 'Dual-network debit card issuance'), there may not be a case for a lower cents-based interchange cap for SNDCs, depending on where the threshold were set; the Board would also consider possible policy measures (for example, somewhat higher interchange caps for small issuers) to offset the cost to small ADIs of supporting two debit networks.

years and represent an increasing proportion of merchant service fees. This has raised concerns that the opacity of scheme fee arrangements may be limiting competitive tension between the card schemes, as well as between acquirers (by obscuring their margins). It could also, in principle, make it easier for schemes to implement fees or rules that may be anti-competitive or have the effect of offsetting or circumventing the Bank's interchange fee regulation. For example, one scheme recently introduced a new fixed scheme fee, levied on acquirers for each physical merchant outlet that they service, regardless of the volume of transactions processed at each location. In principle, fees such as this could reduce competition in the market for debit card payments, because they could be used to incentivise acquirers and merchants to route DNDC transactions to that card scheme (in ways that schemes with less market power cannot match). The Bank previously considered some possible mechanisms for scheme fee transparency as part of the 2007-08 Review, but did not proceed with specific regulatory action. However, in light of recent developments the Board felt it was timely to reconsider requiring greater disclosure of scheme fees, particularly with card payments continuing to increase as a share of retail transactions in Australia.

3.3.2 Reform options

The Bank is consulting on three broad options in relation to scheme fee transparency:

Option 1: No additional disclosure requirements

This option would retain the status quo. The Bank would continue to seek disclosure of scheme fees only as required to assess compliance with net compensation rules.

Option 2: Schemes to publicly disclose all scheme fee rates and rules

Under this option, the Bank would introduce a requirement in the standards for designated card schemes to publish all multilateral scheme fee rates, as well as all scheme rules relating to scheme fees, that apply to Australian scheme participants.

Option 3: Schemes to disclose to the Bank all scheme fee rates and rules, as well as aggregate data on scheme fees paid by Australian scheme participants, with publication of some aggregate data

Under this option, the Bank would – using its information-gathering powers under s26 of the PSRA – require designated card schemes to provide access to all of their multilateral scheme fees, and scheme rules relating to scheme fees, that apply to Australian scheme participants, and to promptly notify the Bank of any changes to these. The Bank would also use its information-gathering powers to collect quarterly data from the card schemes on the aggregate value of scheme fees charged and rebates provided to Australian scheme participants (with the data split into categories based on various characteristics, including at a minimum: issuing and acquiring fees, debit and credit transactions, and domestic and international transactions). Schemes would also be required to provide a list of the top 20 fees by value and the share of total scheme fee revenue that each of these fees account for.

The Bank would consider publishing some of the aggregate data provided by the schemes, if they are sufficiently comparable, to allow the industry to compare the average levels and growth rates of these fees across card schemes. Larger scheme participants would also be required to report annually to the Bank the total scheme fees paid to, and rebates received from, each card scheme they participate in. This information would act as a cross-check on the data reported by the card schemes, and would not be used for publication.

3.3.3 Considerations

The Board generally views transparency as an important mechanism for improving efficiency and promoting competition in the payments system. Many stakeholders were supportive of greater scheme fee transparency, which could lead to a number of benefits. Disclosure requirements could discourage any changes to fee schedules or related rules that may be anti-competitive or could have the effect of circumventing the interchange fee regulations.^{16,17} They would also allow greater visibility over any developments in scheme fees that could push up payment costs, particularly if the competitive pressure arising from DNDCs and LCR were to lessen; for example, industry participants report that over recent years some schemes have progressively increased fees on debit transactions that cannot be routed by merchants, while reducing fees on routable transactions. Greater transparency could also help merchants to better understand the composition of their card payment costs, including the size of acquirer margins. This could increase competitive tension in the acquiring market and allow merchants to make more informed decisions about the payment methods they accept, including regarding transaction routing. Increased visibility of scheme fees could also benefit smaller issuers and acquirers, which generally have less bargaining power with schemes than their larger counterparts.

However, there are some potential drawbacks of greater scheme fee transparency. Most prominently, the international schemes have raised concerns about commercial confidentiality, particularly as scheme fee rebates are typically negotiated on a bilateral basis. In its submission to the Review, Visa also argued that scheme fee disclosure requirements could put regulated card schemes at a competitive disadvantage to schemes that were not subject to the regulation. The Board acknowledged these concerns during its 2007–08 Review, and remains of the view that commercial considerations should be appropriately factored into any requirements for transparency. Greater price transparency can also sometimes have perverse effects on competition and price levels by leading to more implicit price coordination among competitors and less bespoke discounting for different customers.¹⁸

Many stakeholders also pointed out the complexity of scheme fee schedules and the difficulties of ensuring that any disclosures would be useful. Some schemes were said to have hundreds of different scheme fees. If schemes were to publish their entire fee schedules (**Option 2**), it is likely that even payments specialists – let alone non-specialists such as smaller merchants – would find it difficult to understand and effectively make use of this information. Publishing aggregated or averaged data on actual scheme fees paid instead (**Option 3**), may provide industry participants with information that is easier to understand and compare across card schemes. However, reporting methodologies would need to be specified in considerable detail by the Bank to ensure the data were comparable. And given the complexity of scheme fee data, and the associated potential for misreporting, it would be important for the Bank to have access to other information that can be used to cross-check the data.

Compared with the status quo, disclosure requirements would impose some compliance costs on the industry. The compliance burden on schemes to provide the Bank with access to scheme fee schedules and fee-related rules, and notification of any changes to these (**Option 3**), would be low; this is because

16 The net compensation provisions implemented by the Bank following the 2015–16 Review are intended to limit the extent to which schemes can circumvent the interchange benchmarks and caps by increasing the level of scheme fees on acquirers to fund payments and other incentives to issuers.

17 The European Commission (2020), for example, found that the potential merchant savings arising from the interchange caps implemented in Europe in 2015 had been partly offset by higher scheme fees. An international study (CMSPI 2020) also found that higher scheme fees eroded merchant and consumer savings generated by interchange regulation in various jurisdictions.

18 See, for example, Kuhn and Vives (1995) and OECD (2001).

the Bank would simply be seeking the same access and notification that is already provided to scheme participants. However, the schemes would likely need to set up new reporting processes under Option 3, particularly if the scheme fee breakdowns requested by the Bank differed from those that the schemes produce internally. Some issuers and acquirers also noted that it would be challenging to accurately report scheme fees paid and rebates received for different types of card transactions, given the structure and complexity of the schemes' fee schedules and billing arrangements. They indicated that they would incur at least some initial costs to set up data collection and reporting processes if they were required to report this information on an ongoing basis. However, there would be clear overlaps with current internal reporting for net compensation purposes, and a number of institutions have indicated that ongoing compliance costs should be relatively low once reporting processes are set up and automated.

3.3.4 Preliminary assessment

The Board sees considerable merit in providing greater transparency of scheme fees. In addition to better informing merchant negotiations and routing decisions, improved transparency would help shine light on any changes in scheme fee arrangements that might be anti-competitive or seek to undermine the interchange regulations. Greater transparency is unlikely to materialise without policy action.

Requiring card schemes to publish all of their multilateral scheme fees and fee-related rules (**Option 2**) would certainly result in greater transparency. However, the Board acknowledges that there is a degree of commercial sensitivity about scheme fees and rebates, and full transparency might also have perverse effects. The usefulness to stakeholders of the detailed scheme fee schedules – which are much more complex than the schemes' published interchange fee schedules – would also be questionable.

The Board's preliminary view is that **Option 3** would strike an appropriate balance between commercial sensitivity concerns and the benefits of meaningful disclosure to both the Bank and industry participants. Furthermore, stakeholder feedback to date suggests that this option would not create a material compliance burden for the industry, particularly over the medium term once the necessary reporting processes have been established.

3.4 Surcharging

3.4.1 Summary of issues

The Issues Paper noted the Bank's preliminary view that the revised surcharging framework put in place following the 2015–16 Review was functioning well. This framework gives merchants the right to levy a surcharge to recover the cost of accepting payments in designated card schemes, with the ACCC having enforcement powers to prevent merchants from surcharging excessively.¹⁹ Most stakeholders were also of the view that the current surcharging framework is working reasonably well and, as a result, the Board is not proposing to make changes to the surcharging arrangements that were introduced following the previous review.

The Bank also sought stakeholder views on the specific issue of the no-surcharge rules imposed by providers of buy now, pay later (BNPL) services. BNPL transactions have grown rapidly in recent years and are typically more expensive for merchants to accept than other electronic payment methods such

¹⁹ Several payment schemes that are not formally covered by the Bank's surcharging standard – American Express, Diners Club, UnionPay and PayPal – have voluntarily modified their surcharging rules to be consistent with the standard.

as cards. The Bank has long been of the view that the right of merchants to pass on costs to users of more expensive payment methods promotes competition and efficiency in the payments system, which was the rationale for the Bank's previous policy action to remove the no-surcharge rules of card schemes. However, the Bank also recognises that no-surcharge rules can, in certain circumstances, promote competition and innovation in the market for payment services by helping newer providers enter the market and compete with incumbents. The main question the Board has considered as part of this Review is whether there is a public policy case to require the removal of no-surcharge rules in BNPL schemes. The Board has also considered what factors might help determine the point at which a case for policy intervention could emerge in the future and which providers any policy requirement should apply to.

3.4.2 Considerations

The right to surcharge promotes payments system competition and efficiency

As noted, the Board's long-standing view is that the right of merchants to apply a payment surcharge promotes payments system competition and keeps downward pressure on payment costs for businesses. If a business chooses to apply a surcharge to recover the cost of accepting more expensive payment methods, it results in more transparent price signals and may encourage customers to use a cheaper payment option. In addition, the possibility that a customer may choose to use a lower-cost payment method when faced with a surcharge puts competitive pressure on payment providers to lower their merchant costs, and may help merchants in negotiating lower prices directly with their payment providers. By helping keep merchants' costs down, the right to apply a surcharge means businesses can offer a lower price for goods and services to all of their customers and thereby reduce the extent to which users of lower-cost payment methods are cross-subsidising users of more expensive payment methods.

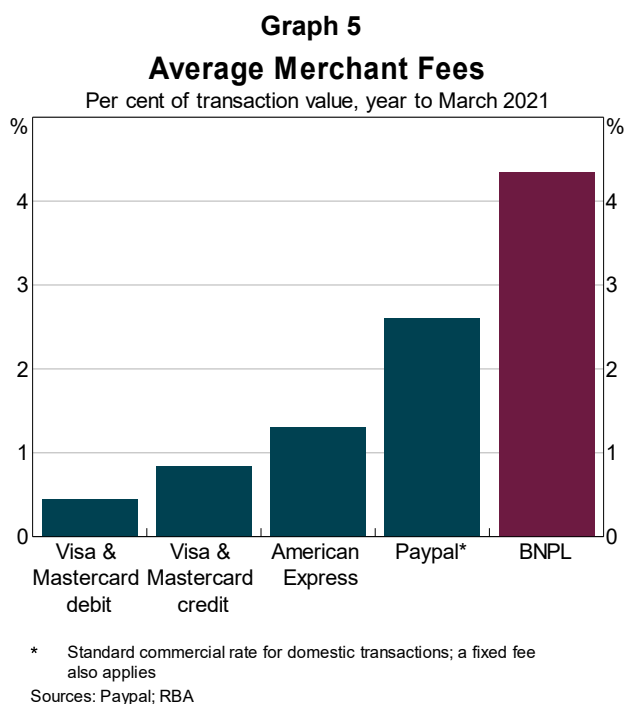
The ability to surcharge can be particularly important for promoting competition between payment schemes in cases where merchants consider it essential to accept a particular payment method for them to remain competitive – that is, if the merchant is of the view that it cannot refuse to accept a payment method in case it loses sales to competitors that do so. In this case, the possibility of surcharging can put competitive pressure on payment providers to keep their costs down, where otherwise there may not have been as much pressure.

The important role that the right to surcharge – even if merchants choose not to exercise that right – can play in bringing down payment costs has been borne out by experience since the Bank's card payments reforms in the early 2000s. These reforms, which included regulation of interchange fees and the removal of no-surcharge rules in the designated Visa and Mastercard systems, led to a significant reduction in merchant service fees in these international card schemes (see Graph 1 in the 'Dual-network Debit Cards and Least-cost Routing' section). Moreover, despite the fact that they were not regulated, average merchant service fees for American Express credit card transactions have also declined significantly since the early 2000s. This partly reflected the ability of merchants to surcharge these transactions after American Express agreed to remove its no-surcharge rule.

In considering whether there is a policy case to require BNPL providers to remove their no-surcharge rules, one challenge has been the lack of comprehensive, timely and consistent data on the Australian BNPL market, including limited data on merchant fees. Accordingly, the Bank recently asked a number of BNPL providers to submit a range of data to the Bank; at the time of writing, 9 of these providers,

including the largest BNPL operators in Australia, had provided data. These data include average merchant fees, as well as transactions and the size of customer and merchant networks.

Based on these data, the (weighted) average BNPL merchant fee was around 4½ per cent in the year to March 2021, compared with an average fee of less than 1 per cent if the same payment were made directly with a Mastercard or Visa credit card (Graph 5). Some stakeholders have observed that the cost of accepting retail payments via individual BNPL services can be significantly higher than this average – sometimes up to 6 or 7 per cent of the value of retail transactions – and that smaller merchants tend to pay higher rates than larger merchants to accept BNPL payments.²⁰



No-surcharge rules have implications for competitive neutrality

A range of stakeholders – including banks and card schemes – have argued that BNPL providers should be required to remove their no-surcharge rules on competitive neutrality grounds. That is, the no-surcharge rules are viewed as giving BNPL providers an unfair competitive advantage over entities, such as card schemes, that are prohibited from imposing no-surcharge rules on merchants (either by regulation or because they have entered into a voluntary undertaking with the Bank). However, BNPL providers argued that the industry is still an emerging and highly competitive part of the retail payments landscape and remains small relative to the size of other electronic payment methods. They argued that merchants therefore have discretion over whether or not to accept BNPL services, so removal of no-surcharge rules is not warranted.

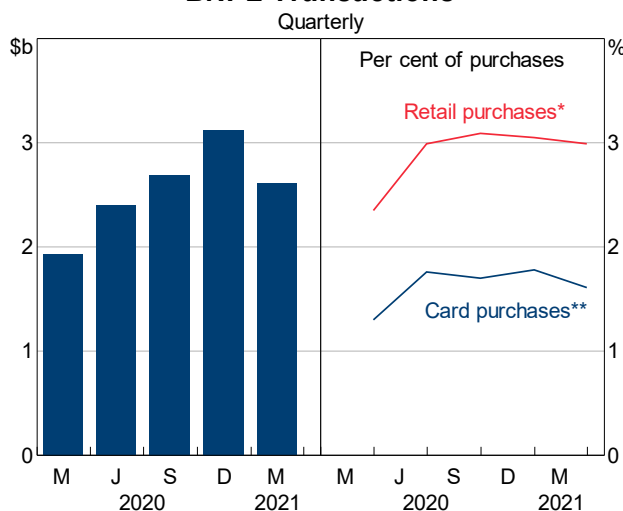
The BNPL sector has grown rapidly in recent years.²¹ It is estimated that BNPL providers processed almost \$11 billion of transactions in Australia in the year to March 2021 (based on the data recently collected by the Bank; see above). Publicly available data for a smaller group of listed providers indicate that transaction values have almost tripled (albeit from a low base) in the past two financial years. This rapid growth indicates that BNPL is increasingly viewed by consumers as a convenient way of making

²⁰ This is also often the case with card payments (see Occhiutto (2020)).

²¹ For further discussion of developments in the BNPL market, see Fisher, Holland and West (2021).

purchases. Another factor that appears to have supported recent growth in BNPL payments is the changes in consumer payment behaviour associated with the COVID-19 pandemic. In particular, there has been a pickup in the share of retail purchases being made online, where BNPL is a more commonly used and accepted payment option.²² Indeed, it is estimated that almost 80 per cent of BNPL transactions are made online.

Graph 6
BNPL Transactions



* Includes both retail and non-retail BNPL transactions
 ** Credit, debit and prepaid card transactions on Australian-issued cards; includes commercial transactions for debit and prepaid cards
 Sources: ABS; RBA

Despite the rapid recent growth, the available evidence indicates that BNPL still accounts for a relatively small share of overall consumer payments in Australia. The value of BNPL transactions was estimated to be equivalent to 1.7 per cent of the value of all Australian debit and credit card purchases in the year to March 2021 (Graph 6). However, BNPL accounts for a higher share of online transactions and has gained considerable traction in certain retail segments. It is estimated that the value of BNPL purchases was equivalent to around 3 per cent of total retail purchases in the year to March.²³ Looking ahead, BNPL will become a more prominent part of the consumer payments market if use and acceptance continue to grow strongly. One of the factors that could support future growth is that newer BNPL business models have emerged that enable transactions at a wider range of merchants, including via the use of virtual cards that are accepted at most merchants that take Mastercard and Visa cards. Another recent development with parallels to earlier developments in the credit card market is that some BNPL providers have begun offering rewards programs to incentivise consumers to use their services, with the cost of such programs likely incorporated into merchant fees.

While the ability of merchants to surcharge can promote a more competitive and efficient payment system, under some circumstances no-surcharge rules can support the development of new payment methods. This is because payments is a two-sided network industry in which service providers must build up both sides of their network – consumers and merchants – to be able to compete successfully. The more consumers in the network, the more valuable it is likely to be to merchants and vice versa.

22 For example, based on the ABS's measure of online retail sales, as a proportion of total retail sales.

23 'Retail purchases' here is measured as retail trade in the ABS Retail Trade release. Retail trade includes purchases of goods (and some food-related services) by consumers, but does not include consumer purchases of most other services such as health, education and travel.

No-surcharge rules may promote innovation and competition by helping an emerging payment service provider develop its network – for example, by making the service initially free or inexpensive for consumers. However, as a payment service becomes more widely used by consumers and accepted by merchants, the potential benefits arising from no-surcharge rules are likely to decline relative to the costs of those rules, including in terms of the competitive impact on other providers and efficiency of the payments system. Accordingly, there is a balance to be struck between a regulatory environment that supports the ability of new payment service providers to compete with larger incumbents and providing newer players with an unfair competitive advantage over the medium term.

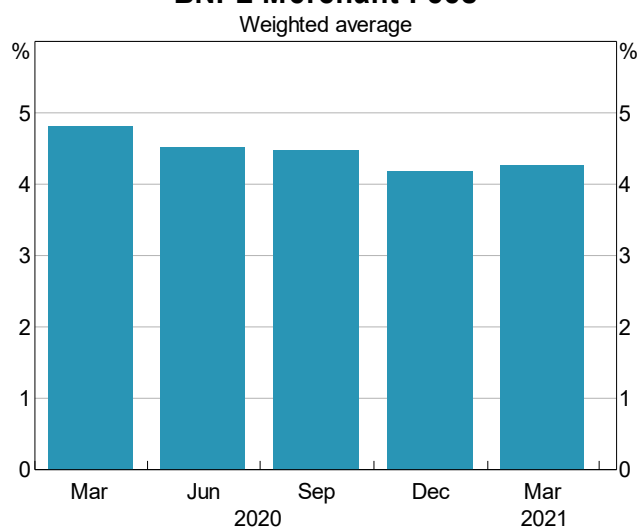
Competition could lead to downward pressure on merchant fees

There has recently been considerable activity in the BNPL market. A number of Australian and overseas companies have entered the domestic market and the variety of services offered by BNPL providers has expanded. It is estimated that there are around 20 BNPL services in the Australian market offered by more than a dozen providers, whereas there was only a small handful of providers a few years ago. Some of the more established BNPL providers have also increased their range of services and other providers of payment services, including banks, have launched products that have similar features to BNPL. In this environment, it is possible that increased competition in the BNPL market could help put downward pressure on merchant fees, potentially reducing the need for regulatory intervention on no-surcharge rules.

There are limited data available with which to assess the effect of competition on BNPL merchant fees. Based on the data provided to the Bank by a number of BNPL providers, the (weighted) average merchant fee across the sector was 4.3 per cent of the transaction value in the March quarter 2021, compared with 4.8 per cent a year earlier (Graph 7). However, some stakeholders have observed that there can be considerable variation both in the fees charged to particular merchants and across individual BNPL providers. It is also worth noting that while merchant fees are a key indicator of competition in the BNPL market, there may also be non-price elements to competition, such as the provision of additional benefits or services to merchants.

Stakeholder views were mixed on the question of whether competition in the BNPL market was resulting in lower merchant fees. Some stakeholders observed that the influx of newer entrants was resulting in increased price competition and noted that some newer providers tended to charge lower fees than established providers. However, others noted that it was difficult for merchants to stop accepting payments from certain established BNPL providers, some of which reportedly charge relatively high fees. Some merchant representatives noted that there was increasing pressure on merchants to offer a range of BNPL payment options to meet customer preferences, which could dull the effects of price competition between providers.

Graph 7
BNPL Merchant Fees



Source: RBA

Potential policy approach to BNPL no-surcharge rules

If the Board were to reach the conclusion that it would be in the public interest for one or more BNPL providers to remove their no-surcharge rules in order to promote competition and efficiency in the payments system, there are a number of options that could be considered. The Board's preferred approach would be to seek a voluntary agreement from the relevant provider(s). This would be consistent with the approach that has been taken in relation to a number of other payment schemes in the past that have removed their no-surcharge rules, including American Express and PayPal.

In the event that a voluntary agreement was unable to be reached, the Bank could potentially seek to use its powers under the PSRA to impose a standard that would prevent a BNPL provider from imposing no-surcharge rules on merchants. Some BNPL providers have questioned the Bank's ability to regulate in this area on the basis that BNPL arrangements may not meet the definition of a 'payment system' and/or that providers of these arrangements may not be 'participants' in payment systems. The Bank has raised this issue in the context of the current Treasury Review of the regulatory architecture for the payments system and will continue to discuss it with the Australian Government. The payments system has become more complex over time and BNPL providers are one example of an increasing range of entities that are playing a material role in facilitating payments. The Bank believes such entities should be able to be regulated if doing so would be in the public interest in terms of promoting competition and efficiency and controlling risk in the payments system. The Bank's submission to the Treasury Review suggested that there may be scope to clarify how these entities should be treated under the PSRA. It may also be necessary to consider amendments to the PSRA to ensure that BNPL providers could be subject to appropriate regulation in the event that the Board concluded that regulatory intervention was in the public interest.

Prevention of excessive surcharging

If the Board were to reach the view that it was in the public interest to require certain BNPL providers to remove their no-surcharge rules, it would be important to develop a framework to prevent excessive surcharging of customers. This raises the question of what might be an allowable surcharge. It would be important that the allowable surcharge was clearly defined and observable, as is the case for card

schemes under the relevant standard (Standard No. 3 of 2016). One option could be that merchants would have the right to surcharge up to the total cost of accepting the particular BNPL service. That is, if a merchant were charged a per transaction fee of, say, 6 per cent for accepting a payment via a particular BNPL service, the merchant would have the right to levy up to a 6 per cent surcharge on consumers who benefit from using that service. As is the case for card schemes where surcharging is permitted, merchants would not be required to surcharge BNPL transactions but would have the choice.

BNPL providers have, however, argued that this would not be an appropriate approach towards surcharging because their fees represent the cost of a range of services provided to merchants (such as marketing and lead referrals), not just payment processing. The Bank has previously considered similar arguments made by credit card schemes, some of which also provide advertising and marketing services to merchants, but reached the judgement that the lack of price signals would have substantial adverse consequences for efficiency of the payments system. It is also worth noting that merchants may choose not to exercise the right to surcharge if they perceive that they benefit significantly from these types of non-payment services.

An alternative approach to surcharging could be to limit the allowable surcharge to the 'payment' component of a merchant's cost of accepting BNPL payments. While some stakeholders have argued that this approach to surcharging could conceptually be more appropriate, it is unclear how the payments component of BNPL merchant fees could be measured in a context where BNPL providers do not provide separate services and prices for the payments and non-payments components of their offerings.

A further complication in this area is the potential interaction between merchant surcharging of BNPL transactions and the *National Consumer Credit Protection Act 2009* (NCCPA). BNPL services often have one or more features that result in them falling within regulatory exemptions from the NCCPA, as set out in the National Credit Code administered by ASIC. Some stakeholders are of the view that if merchants were to levy a surcharge on consumers who use BNPL services, it could result in the BNPL provider no longer qualifying for certain regulatory exemptions. The Bank will continue to work with the Australian Government and ASIC as necessary, with a view to clarifying this issue.

3.4.3 Preliminary assessment

The Board's preliminary assessment is that BNPL providers in Australia have not yet reached the point where there is a clear public interest case for requiring them to remove their no-surcharge rules. However, the arguments are finely balanced and the Bank intends to keep this issue under review in light of market developments and broader developments in the payments system.

Some BNPL providers are growing very rapidly and are becoming widely accepted in certain sectors, particularly for online payments, and a large number of consumers have adopted BNPL services. A number of stakeholders were of the view that it was increasingly difficult for merchants not to accept BNPL for competitive reasons and others have raised concerns about no-surcharge rules creating an uneven playing field with regulated schemes. However, as noted earlier, BNPL still accounts for a relatively small share of consumer transactions compared with other electronic payment methods such as cards, despite the recent strong growth. The BNPL industry is also evolving rapidly and it is possible that the array of new providers will put competitive pressure on merchant costs. Consistent with its long-standing approach of intervening only when there is a clear public interest case to do so, the Board does not propose that any BNPL providers be required to remove their no surcharge rules at this time.

However, the Board considers that a case for seeking the removal of one or more BNPL providers' no-surcharge rules could emerge before too long if these services continue to grow rapidly and become an

even more prominent part of the retail payments landscape. The Board is also conscious that the payments industry is developing quickly and the approach to this policy issue should take into account the possibility of other innovative payment methods emerging over time. Accordingly, the Bank intends to periodically review the case for the removal of no-surcharge rules in BNPL schemes and in any other emerging payment methods.

Proposed approach to review of no-surcharge rules

A number of potential approaches to assessing the point at which it would be in the public interest for BNPL providers (and/or other emerging payment methods) to remove their no-surcharge rules could be considered. One approach would be to use relatively simple numeric thresholds – for example, transaction values or market shares – as a trigger for policy intervention. While this may have the benefit of simplicity and transparency, the Board considers that it would be preferable to take into account a range of relevant information, including both quantitative indicators and qualitative factors. This conclusion partly reflects the difficulty of measuring and calibrating potential regulatory thresholds and determining how much weight to place on them, as well as the Board’s view that considerable judgement and engagement with a range of stakeholders will be necessary to inform the Bank’s assessment.

Accordingly, it is envisaged that the Bank’s assessment of policy in relation to no-surcharge rules will be broadly guided by four main considerations (or criteria):

1. The amount of transactions processed via a payment method relative to other payment methods.
2. The share of consumers and/or merchants that have adopted a payment method.
3. The extent to which no-surcharge rules create an uneven playing field in the payments system.
4. The degree of competition in the relevant market for payment services and developments in payment costs.

Criteria 1 and 2 relate to the significance of different payment methods in the retail payments system. It would be expected that the greater the share of consumer payments that are made via a particular payment service, the more difficult it would be for merchants to decline to accept it for competitive reasons. In assessing a payments provider against criterion 1, the Bank would likely take into account its market share in particular segments (e.g. online or in-store) as well as in the system as a whole. Similarly, a payment method would more likely be considered to be an essential payment offering the greater the share of merchants that accept it and the more consumers that use the payment method (criterion 2). The Bank would also take into account competitive neutrality arguments (criterion 3) – that is, whether no-surcharge rules confer an undue competitive advantage for some payment providers over other providers that are subject to the Bank’s surcharging regime. Competition and developments in payment costs (criterion 4) would factor into the Bank’s assessment given the potential for competition to exert downward pressure on merchant fees without the need for intervention on no-surcharge rules. The Bank’s assessment would also take account of any other factors that are deemed relevant to determining whether the removal of no-surcharge rules is in the public interest. One such factor that may be relevant is whether other BNPL providers have already removed their no-surcharge rules. For example, if the Board had already determined that there was a case for a BNPL provider to remove its no-surcharge rules, the bar for taking action on other (smaller) providers may be lower on competitive neutrality grounds.

While the Bank will consider a range of information in reviewing the case for removing no-surcharge rules of BNPL providers, it expects to focus on a number of key indicators that relate to the criteria above. These indicators, which are based partly on the availability of relevant data, are expected to include:

- the number and value of BNPL payments relative to measures of economy-wide consumer transactions such as total card payments and retail trade. As noted, shares in significant segments such as online payments are also likely to factor into the Bank’s assessment.
- the size of BNPL schemes compared with regulated card schemes – for example, measured by transactions as well as customer and merchant networks.
- the number of consumers that have adopted a BNPL service, including as a proportion of the adult population and relative to other electronic payment methods. It would be expected that the more consumers that have adopted a particular payment method, the more likely it would be that a merchant feels obliged to accept it.
- the size of a BNPL provider’s merchant network, including in comparison to the number of retail businesses operating in Australia. This is an indicator of how widely a particular BNPL service can be used.
- developments in BNPL merchant fees as an indicator of whether market forces are leading to downward pressure on merchants’ cost of acceptance.

The Bank’s preliminary assessment is that some BNPL providers could already be considered widely available and accepted payment methods on the basis of their customer and merchant networks. For example, there were around 5 million active BNPL customer accounts at the end of the March quarter and around 105,000 merchant accounts (Table 2).²⁴ Based on publicly available data, the largest Australian BNPL provider had around 3.5 million customers and 58,000 merchant accounts in Australia and New Zealand as at 31 March 2021. However, as noted earlier, shares of transaction flows remain quite small relative to some other electronic payment methods and it is possible that competition could lead to lower merchant costs without the need for regulatory intervention. Consistent with the Bank’s approach of regulating only when it is clear that doing so would be in the public interest, the Board will continue to monitor these indicators (as well as other relevant information) and keep the policy position on BNPL providers’ no-surcharge rules under review (as discussed above).

Table 2: Indicators of BNPL Sector
Industry total, year to 31 March 2021^(a)

Value of BNPL transactions \$ billion	Value of BNPL transactions Per cent of value of domestic consumer card payments ^(b)	Value of BNPL transactions Per cent of value of ABS retail trade	Active customer accounts^(c) Millions, as at 31 March 2021	Active customer accounts Per cent of adult population ^(d)	Merchant accounts^(d) '000s, as at 31 March 2021	Merchant fees, weighted average (%)
10.8	1.7	3.0	5.0	24	105	4.4

(a) Calculated from data provided to the RBA by 9 providers.

(b) Credit, debit and prepaid card transactions on Australian-issued cards. Includes commercial transactions for debit and prepaid cards.

(c) Active customers defined as having made at least one transaction in the past 12 months.

(d) As at September 2020. Note that individual consumers and merchants may have accounts with more than one provider. Adult population refers to ABS estimated resident population aged 18 years and older.

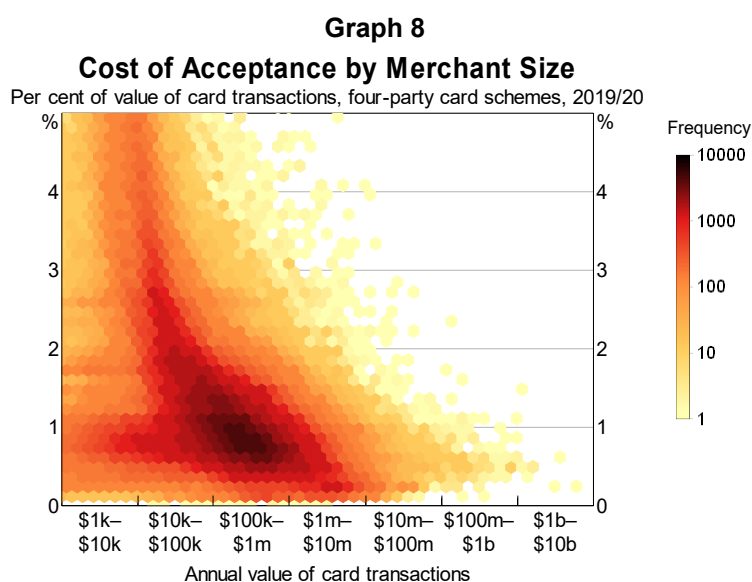
Sources: ABS, RBA

24 Merchant numbers do not include acceptance of BNPL virtual cards.

3.5 Competition in Card Acquiring

3.5.1 Summary of issues and considerations

The Issues Paper noted that there appear to be some ongoing impediments to competition in the acquiring market, particularly in respect of services provided to smaller merchants. Merchant service fees charged to smaller merchants tend to be significantly higher and much more widely dispersed than those faced by larger merchants (Graph 8). In 2019/20, the average cost of acceptance for four-party scheme cards was around 1.5 per cent for merchants with less than \$100,000 in annual card transactions, and 0.9 per cent for merchants with \$100,000 to \$1 million in card transactions. In contrast, merchants with more than \$10 million in card transactions had an average cost of acceptance of less than 0.6 per cent. Some of this difference in merchant service fees could be explained by cost-related factors, such as economies of scale for acquirers in providing payment services to merchants with larger transaction volumes and the ability of larger merchants to negotiate 'strategic' interchange rates with the card schemes. In some cases, larger merchants may also be charged lower fees due to a relatively lower risk profile. However, impediments to competition in the acquiring market also appear to be an important factor.



Source: RBA

Submissions to the Bank indicated mixed views on this issue. Many stakeholders argued that competition and innovation in the acquiring market is strong. They pointed to a range of new technology-focused firms entering the market in recent years, narrow acquirer margins and high rates of switching – including among smaller merchants. Some stakeholders also noted that the reforms implemented by the Bank as part of the 2015–16 Review – which sought to improve the information available to merchants about their payments costs – have made it easier for merchants to seek quotes from alternative providers.²⁵

However, other submissions pointed to various factors impeding competition. One issue raised was that switching to a new acquirer can be costly and operationally complex. This may be due to one-off transitional costs, such as those associated with replacing card terminals and re-integrating back-office

²⁵ Under the reforms, acquirers and payment facilitators are required to provide monthly and annual statements to merchants detailing their costs of acceptance for each card payment card system regulated by the RBA.

systems. Alternatively, given that payment services are often ‘bundled’ with other banking services, merchants might lose access to preferential rates on business banking services such as credit facilities if they source their payments services from another acquirer.

Another issue is that price transparency is still relatively limited. Most acquirers only publicly advertise their fixed-rate or ‘simple merchant plans’, where merchants pay either the same rate per transaction or a fixed dollar amount per month, irrespective of the type of cards used by their customers.²⁶ More competitively priced plans are usually negotiated on a bespoke basis between the acquirer and the merchant. In some cases, acquirers require detailed card transaction information from merchants (such as the shares of standard and premium, and domestic and international card transactions) to determine the most competitive plan and pricing. While this information is available to the incumbent acquirer, it is not typically included in the standard cost of acceptance statements provided by that acquirer, and can be difficult for a merchant to source. This opacity in acquirers’ pricing models and lack of access to transaction data makes it difficult for merchants to compare different plans and acquirers and shop around for a better deal.

There also appear to be some frictions in the market related to behavioural factors. The complexity of payments concepts and the difficulty that merchants face in understanding and comparing acquirers’ offerings generate considerable inertia in merchants’ choice of payment plans and acquirers.²⁷ These challenges may cause merchants to remain with their existing provider even if they could achieve significant net benefits from switching. This, in turn, might limit the competitive pressures in the acquiring market that would result from merchants more regularly switching providers.

3.5.2 Preliminary assessment

The Bank’s reforms following the 2015–16 Review have significantly improved the information available to merchants about their payment costs. However, the Board’s preliminary assessment is that price transparency should be further enhanced to help reduce some of the remaining impediments to competition in the acquiring market for smaller merchants. Accordingly, the Bank is proposing two initiatives.

First, the Bank intends to regularly publish summary information on merchant service fees for merchants of different sizes. This would be based on merchant-level data on payment costs collected from a sample of acquirers on an annual basis (these data are already collected on an ad hoc basis). The pricing information would be accompanied by educational material about key concepts in card payments and acquiring services. The aim is to increase merchants’ awareness of the pricing available in the market, improve their understanding of different types of merchant plans and payments services, and ultimately make it easier for merchants to search for a cheaper plan or negotiate a better deal with their existing acquirer. To ensure this information is easily accessible to merchants, acquirers and other entities that provide card acceptance services would be expected to notify their merchant customers about where to find the information at least once a year, likely at the same time as they provide the

26 Fixed-rate (or bundled) plans charge the same percentage rate for each card transaction, irrespective of the card scheme or type of card. Simple merchant plans typically charge a fixed monthly fee which covers a certain value of transactions (for example, \$30 for up to \$1,500 of card transactions) within a month, with the merchant then paying a fixed percentage fee (often around 1.5 per cent) for any additional transactions above the limit.

27 Many of the behavioural frictions observed in the acquiring market are similar to those that arise in some consumer markets like the energy and mortgage markets. Some frictions related to consumer comprehension of pricing information were explored in a recent study to help inform the implementation of the Australian Energy Regulator’s Retail Pricing Information Guidelines and the ACCC’s Electricity Retail Code (Behavioural Insights Team (2020)).

annual cost of acceptance statement.²⁸ This would act as a periodic prompt or ‘nudge’ for merchants to review their payments services, and potentially reduce some of the inertia in the market.

The Bank is also exploring with Treasury and the ACCC the possibility of extending the Consumer Data Right (CDR) to acquiring services provided to small businesses. The CDR is currently being rolled out for consumer banking services, where it is known as Open Banking, and was specifically designed to address the types of market inefficiencies that are evident in the acquiring market. The CDR could make it easier for merchants to seek quotes from alternative payments service providers by allowing them to easily source and share their detailed card transaction data. Over the longer term, third-party providers offering comparison (and possibly switching) services could also emerge, further reducing merchants’ search and switching costs.

The Bank has already consulted with a wide range of stakeholders on these initiatives. The initial feedback suggests that these initiatives would benefit competition while imposing a relatively limited additional regulatory burden on acquirers. The Bank is nevertheless open to further feedback on the proposals.

3.6 Net Compensation Regulation

3.6.1 Summary of issues and considerations

The Issues Paper noted that the revised net compensation provisions in the interchange standards have been working effectively. The Board, however, is aware of several issues relating to the operation of these provisions, based on feedback from the 2019/20 annual certification process for net compensation as well as broader engagement with schemes and issuers.

The first issue is that the standards do not expressly state when a new issuer must begin certifying its compliance with the net compensation provisions, and certifications for the year to June 2020 indicated that interpretation of the standards on this point varied across different schemes and issuers. Accordingly, the Bank provided guidance in January to clarify its expectation that:

1. a new issuer should begin certifying once it has had a full financial year of operation following the public launch of its card product (with the scheme certifying at the same time as the issuer)
2. the new issuer (and scheme) will include in its first certification all issuer receipts and payments relevant to the net compensation calculation that have accrued prior to the first certification.²⁹

In reaching this view, the Bank recognised that new issuers are likely to experience low transaction volumes in the early stages of developing and launching a product to the public. This could result in issuer payments to the scheme being insufficient to offset the benefits that schemes often provide to support the entry of new issuers into the market, even after allowing for the amortisation of such benefits over a number of reporting periods that is already provided for in the standards.

The second issue is whether card migration benefits should be excluded from issuer receipts in the net compensation provisions. Migration benefits are payments by a scheme intended to compensate an issuer for all or part of the cost of switching schemes (such as the cost of re-issuing cards). They meet the current definition of an issuer receipt, because they can incentivise entry into a contract for issuing

²⁸ Merchants sometimes procure their card acceptance services indirectly from a payment facilitator, independent sales organisation (ISO) or other payment service provider, rather than directly from an acquirer. Where this is the case, these entities typically provide their merchant customers with monthly and annual cost of acceptance statements, so the Bank envisages they would also provide the new pricing and educational information.

²⁹ See RBA (2021a)

cards of a scheme.³⁰ However, some stakeholders have expressed a concern that including migration benefits in net compensation calculations may create a disincentive for issuers to switch schemes, as it makes it more difficult for the new scheme to match, or exceed, the total value of *other* benefits offered by the incumbent scheme; this potentially reduces competition between card schemes for issuing arrangements.

Finally, the Bank has identified a couple of issues relating to the definition in the standards of a ‘Core Service’ – the fee for which can be included as an issuer payment in net compensation calculations. The first is that part (a) of the definition in Standard No.2 of 2016, which pertains to both debit and prepaid cards, suggests that only payments for services related to debit cards are issuer payments. The Bank’s intent however, is that payments related to prepaid cards should also be treated as issuer payments (provided they meet the other elements of the definition). In their net compensation certifications, schemes and issuers have interpreted ‘Core Service’ in line with this intent. Second, the Bank is concerned that, as schemes become involved in more parts of the payments value-chain, ‘Core Service’ (under both Standard No.1 and Standard No. 2 of 2016) could in some cases be interpreted widely to include services that are provided by the schemes but that would traditionally have been performed by issuers themselves, or by third parties (for example, account maintenance, or the transaction authorisation usually performed by the issuer). This would inflate issuer payments, allowing schemes to provide additional benefits to issuers.

The Issues Paper also considered what actions the Bank should take, or should have the power to take, following any breach of the net compensation provisions, particularly given that some enforcement actions could have the effect of rewarding a scheme for a breach. For example, requiring an issuer to ‘undo’ the breach by repayment or adjustment to an accrued entitlement would result in the scheme recouping some of the cost of the high up-front incentives it offered to secure the issuing contract. The appropriateness of the Bank’s enforcement powers under the PSRA was also raised more generally: see the section on ‘Regulation and enforcement’ below. Related questions were whether greater obligation should be placed on schemes to comply with the net compensation provisions (currently the substantive obligations rest with the issuers) and whether the current enforcement options available in the case of a breach should be expanded.

3.6.2 Preliminary assessment

The Board’s view is that the graduated approach to certification by new issuers, as set out in the Bank’s recent guidance, supports new entry and competition in the issuing market. The Board therefore intends to amend the standards to formalise these certification requirements for new issuers. Their inclusion in the interchange standards will bring greater regulatory clarity for issuers entering the market.

The Board does not see a strong case for excluding card migration benefits from net compensation calculations. The Board acknowledges the concerns raised by some stakeholders, but its preliminary view is that it is unlikely to have a material effect on competition. Rather, the exclusion of such benefits would be inconsistent with the broader intent of the standards to limit interchange-like payments to issuers, and would introduce additional complexity and potential loopholes into the regulation.

In relation to the definition of ‘Core Service’ in Standard No.2, the Board supports a minor technical revision to part (a) to include prepaid cards, to bring the drafting into line with the Bank’s intent. Consistent with the conclusions from the 2015-16 Review, the Board also believes that ‘Core Service’

³⁰ As noted in RBA (2019a), p60.

under both standards should be interpreted narrowly, to exclude services that are provided by a scheme, but that would traditionally have been performed by the issuer or a third party.³¹ A wide interpretation is inconsistent with the intent of the standards, as it increases the scope for schemes to provide interchange-like benefits to issuers. This would translate to higher costs for acquirers and merchants, and may provide an advantage to schemes over third-party suppliers (as schemes would be able to reimburse service fees to the issuer).

Lastly, compliance with the net compensation provisions has been satisfactory overall and breaches have been dealt with effectively, despite the Bank's limited enforcement powers under the PSRA. Accordingly, the Board does not propose making changes to the net compensation framework or extending the substantive obligations. However, the question of whether the Bank's enforcement powers should be expanded more generally may be considered by the Treasury Review, as part of its broader assessment of the fitness of the regulatory architecture.

3.7 Other Issues

3.7.1 Digital wallets and mobile payments

In recent years, large multinational technology companies such as Apple, Google and Samsung have launched digital wallets in Australia for use in their respective mobile platforms. These wallets enable consumers to make contactless (and in some cases online) payments with a smartphone or other consumer device³² using a digital representation of their debit and/or credit cards. The contactless functionality of digital wallets is typically facilitated by near-field communication (NFC) technology in mobile devices. All of Australia's major banks and many smaller issuers now support each of the three largest wallets (Apple Pay, Google Pay and Samsung Pay). The use of these wallets by consumers has grown strongly over the past few years. This is evident in the Bank's most recent Consumer Payments Survey, which showed that digital wallet transactions made up 8 per cent of in-person card transactions in 2019, compared with 2 per cent in 2016. In addition, issuers have said that use of digital wallets has continued to grow strongly since the onset of the COVID-19 pandemic, as consumers have shifted towards card payments more broadly.

The Issues Paper noted that mobile platforms take different approaches regarding access to NFC technology for contactless payments. On Android devices, third parties are able to directly leverage NFC functionality to develop their own mobile payment applications that compete with Google Pay or Samsung Pay. In contrast, on the iPhone, direct access to NFC technology for payments is restricted to Apple's 'Wallet' application, meaning third parties are unable to develop their own mobile payments applications for iOS without transactions going via Apple Pay. In submissions to the Review, some stakeholders raised concerns about the ability of mobile platforms to restrict access to the underlying technology used for mobile payments, and restrict the ability of issuers to pass on mobile wallet provider fees to consumers, both of which could restrain competition in the market for digital wallets.

Apple's restriction on access to NFC technology for contactless payments on the iPhone is attracting growing international regulatory scrutiny. The European Commission is currently conducting a formal antitrust investigation into this issue, and is also considering legislation that would ensure third parties could access technologies used for payments (such as NFC) on fair and reasonable terms. German, Swiss and Dutch national authorities have also considered, or are considering, access issues related to NFC.

31 See RBA (2019a), p 18.

32 For example, some smart watches and fitness trackers include digital wallet functionality.

In Australia, the ACCC denied an application by four Australian banks (including three of the major banks) to collectively bargain with Apple over access to the iPhone's NFC chip in 2017; however, Apple Pay was much less widely supported by issuers and used by cardholders at the time. More recently, a Parliamentary Joint Committee has commenced an inquiry into mobile payment and digital wallet financial services, which is considering some of the potential competition issues noted above.

It is possible that regulation could facilitate greater competition in the digital wallet market and improve the ability of issuers to bargain with digital wallet providers. However, regulation would need to also consider any implications for the safety and security of the payments system. Further, regulating in this area would be complex and the Bank's power to do so currently under the PSRA is not entirely clear (although this may be clarified following the Treasury Review, discussed below). With digital wallet transactions still accounting for a small share of overall card payments, the Board does not see a strong case for regulatory action at this stage. However, if the recent strong growth in the use of digital wallets continues, a case for intervention may well emerge, and so the Board will continue to monitor developments in Australia and overseas closely.

3.7.2 Access regimes

Stakeholders have noted that they believe the Bank's revised access regimes for the Visa and Mastercard credit card schemes are working well to support competition from new participants in this market. A range of new issuers and acquirers have entered the Australian market over recent years, many of which are smaller technology-focused firms. As noted in the Issues Paper, the processing of applications for scheme membership occasionally falls outside of the timeframes published on schemes' websites, but this has been attributed to applicants taking additional time to supply the requisite information (for example to demonstrate compliance with anti-money laundering regulation). The Bank has received very few complaints from would-be participants regarding delays in access applications. Accordingly, the Board does not propose to modify the existing access regimes for credit cards.

Access issues related to the NPP were considered in a public consultation conducted by the Bank with input from the ACCC in 2018/19. During this consultation, stakeholders raised a number of concerns about access for new participants, and the Bank made a number of recommendations aimed at addressing some of these concerns in its final report. Following the ACCC's announcement of a decision on the merger application involving NPPA, BPAY and EPA, the Bank will consult with the ACCC regarding the timing of a follow-up review of NPP functionality and access.

3.7.3 Regulation and enforcement

The Issues Paper noted that there are some limitations to the Bank's enforcement powers under the PSRA. For example, the penalty for failing to comply with a direction under section 21 of the Act is substantially lower than penalties for offences under other legislation related to the financial sector. However, there have not been any significant issues regarding compliance with the Bank's standards and access regimes, and stakeholders have noted that good outcomes have been achieved under the existing regulatory framework and enforcement mechanisms. Accordingly, the Board considers that major changes to its enforcement powers are not warranted at this stage.

As discussed above in the section on 'Net Compensation Regulation', the Treasury Review may consider whether the Bank's current enforcement powers remain appropriate. It will also likely consider the scope of the Bank's regulatory powers. The payments system is now more complex and involves a wider range of entities than when the current regulatory framework was put in place in the late 1990s. Many

of the newer participants in the payments system may not fit neatly within the existing regulatory framework. Accordingly, the Bank noted in its submission that the Treasury Review could consider clarifying the PSRA to ensure that all entities that play a role in facilitating payments could be subject to regulation under the Act if it were in the public interest.

3.7.4 American Express Companion Card system

The American Express Companion Card system was designated in October 2015, and Standards No. 1 and No. 3 apply to this system. As noted in the Issues Paper, the major banks have stopped issuing companion cards as a result of the net compensation provisions. Accordingly, the Bank plans to revoke the designation.

4. Summary and Next Steps

The preceding chapter identified a number of areas where there is a case for changes to the existing regulatory arrangements for payment cards. It is the preliminary view of the Board that competition and efficiency in the payments system could be enhanced by:

Changes to card regulations

- replacing the current cents-based debit (and prepaid) interchange fee cap (15 cents per transaction) with different, and lower, caps for DNDCs (10 cents) and SNDCs (6 cents)
- requiring schemes to publish the interchange fees for domestic transactions on foreign-issued cards on their websites
- formalising recent guidance about when and how new issuers should begin certifying compliance with the net compensation provisions of Standards No. 1 and 2 (and including a minor technical revision to the definition of 'Core Service')
- revoking the designation of the American Express Companion Card system

Other policy proposals

- setting an explicit expectation that:
 - the major banks will continue to issue DNDCs, with two card schemes to be provisioned in all form factors, including mobile wallets, offered by the issuer (where the functionality is supported by the scheme)
 - all acquirers and payment facilitators will offer, and promote, LCR functionality to merchants in the device-present environment
 - the industry would follow a set of principles outlined by the Bank regarding the implementation of LCR in the device-not-present environment
- requiring schemes to provide the Bank with access to their fee schedules and all scheme rules (including, but not limited to, rules related to fees), and to notify the Bank promptly of any changes to scheme fees and rules
- collecting quarterly data from card schemes on scheme fee revenue (net of rebates), as well as information on the top 20 fees by value, and annual data from larger issuers and acquirers on scheme fee payments (net of rebates)
- collecting merchant-level data on payment costs from large acquirers each year and using it to publish pricing information and other educational material for merchants (with acquirers expected to notify merchants at least once each year where to find the published material)
- exploring with Treasury and the ACCC the possibility of extending the CDR to acquiring services provided to small businesses.

The Board also wishes to ensure that merchants' eligibility for strategic interchange rates on credit card transactions is not linked to the value or volume of their debit card transactions. However, at this stage the Board is agnostic on whether this is best achieved through voluntary undertakings with the schemes, or by introducing a new standard expressly prohibiting any such tying conduct. If, following this consultation, the Board decides to consult on a new standard, the Bank will conduct a separate consultation on the draft new standard. To be clear, a new standard prohibiting tying conduct is not part of this consultation (and so is not included in Appendix B).

The Board does not propose that BNPL providers be required to remove their no-surcharge rules at this time. However, the Bank will continue to monitor developments in the industry and will review the case for the removal of no-surcharge rules in emerging payment methods, including BNPL schemes, on a regular basis. The Bank will adopt a principles-based approach to reviewing no-surcharge policies in emerging payment methods.

The Bank is seeking comments on these policy proposals and the draft varied standards set out in Appendix B, which incorporate the relevant changes above. The draft variations to the standards are also described below.

1.1 Draft Standards

Reflecting the Board's preliminary view, draft variations to the Bank's standards have been prepared that would give effect to a set of reforms with the above elements.

Appendix B presents draft variations to the following existing standards:

- *Standard No. 1 of 2016: The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers*
- *Standard No. 2 of 2016: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers*
- *Standard No. 3 of 2016: Scheme Rules Relating to Merchant Pricing for Credit, Debit and Prepaid Card Transactions.*

Draft Standard No. 1: The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers

This standard would apply to the MasterCard Credit Card System and the Visa Credit Card System. The proposed variations:

1. remove references to the American Express Companion Card system
2. require schemes to publish the interchange fees for domestic transactions on foreign-issued cards on their websites
3. formalise recent guidance about when and how new issuers should begin certifying compliance with the net compensation provisions (with a minor technical revision to the definition of 'Core Service').

Draft Standard No. 2: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers

This standard would apply to the eftpos, MasterCard and Visa debit card and prepaid card systems. The proposed variations implement the second and third changes described above for credit cards, and

replace the current cents-based debit (and prepaid) interchange fee cap (15 cents per transaction) with different, and lower, caps for DNDCs and prepaid cards (10 cents) and SNDCs (6 cents).

Draft Standard No. 3: Scheme Rules Relating to Merchant Pricing for Credit, Debit and Prepaid Card Transactions

This standard would apply to the MasterCard and Visa credit card systems, and the eftpos, MasterCard and Visa debit card and prepaid card systems. The proposed variations remove references to the American Express Companion Card system.

4.2 Issues for Consultation and Next Steps

The Bank is seeking submissions on the options in Chapter 2 and, in particular, the Board's preferred options, including those embodied in the draft standards. Submissions are requested by 9 July 2021. The Bank will then hold meetings with interested stakeholders. The Board will then assess feedback received and expects to take a final decision on changes to the interchange standards at its August or November meeting.

Stakeholders are encouraged to focus not only on the broad approach, but also on the detailed drafting of standards. In preparing submissions, stakeholders should consider the following general questions:

1. Is the proposed approach appropriate? Does it meet the public interest?
2. Do the draft standards achieve what is intended?
3. Are there factors that have not been properly addressed or considered, either in the general approach or the specific drafting?
4. What impact will the proposed policy changes have on your regulatory compliance costs? (Please provide dollar estimates.) Are there alternatives that would achieve the policy objectives at lower cost?
5. How much time should be allowed between any final decisions being made on the interchange standards and the effective date of any new or revised standards? What factors are relevant to the length of this implementation period?

5. Consultation

The Board is seeking views from interested parties on this Consultation Paper. Formal written submissions on the options discussed in Chapter 2 and on the draft standards in Appendix B, or on any other aspect of the Bank's card payments reforms, should be provided by no later than 9 July 2021, and should be sent to:

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

or

pysubmissions@rba.gov.au

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.

Submissions will be published on the Bank's website, unless the Bank determines that there are reasons not to do so. Where some elements of a submission are considered confidential, respondents are requested to provide two versions of the submission – one for consideration by the Bank and one, with confidential information removed, for publication. In the normal course of events, those making submissions will be provided with an opportunity to discuss their submission with the Bank.

Reserve Bank of Australia
May 2021

Privacy

Unless requested otherwise, published submissions will include contact details and any other personal information contained in those documents. For information about the Bank's collection of personal information and approach to privacy, please refer to the Personal Information Collection Notice for Website Visitors and the Bank's Privacy Policy, which are both available at <http://www.rba.gov.au/privacy>.

References

- ACCC (Australian Competition and Consumer Commission) (2021)**, 'Visa undertakes to address competition concerns over debit card payments', Media Release No 20/21, 10 March. Available at <<https://www.accc.gov.au/media-release/visa-undertakes-to-address-competition-concerns-over-debit-card-payments#:~:text=The%20ACCC%20has%20accepted%20a,its%20dealings%20with%20large%20merchants.>>>.
- Behavioural Insights Team (2020)**, 'Testing comprehension of the reference price', 26 June. Available at <<https://www.aer.gov.au/system/files/Testing%20Comprehension%20of%20the%20Reference%20Price.pdf>>.
- Black Economy Taskforce (2017)**, 'Final Report', October. Available at <https://treasury.gov.au/sites/default/files/2019-03/Black-Economy-Taskforce_Final-Report.pdf>.
- Caddy J, L Delaney and C Fisher (2020)**, 'Consumer Payment Behaviour in Australia: Evidence from the 2019 Consumer Payments Survey', RBA Research Discussion Paper No 2020-06.
- CMSPi (2020)**, 'Global Review of Interchange Fee Regulation', 2 December. Available at <<https://cmspi.com/eur/resources/download-global-interchange-report/>>.
- European Commission (2020)**, 'Report on the application of Regulation (EU) 2015/751 on interchange fees for card-based payment transactions', 29 June. Available at <https://ec.europa.eu/competition/sectors/financial_services/IFR_report_card_payment.pdf>.
- Fisher C, C Holland and T West (2021)**, 'Developments in the Buy Now, Pay Later Market', RBA *Bulletin*, March, viewed 20 April 2021. Available at <<https://www.rba.gov.au/publications/bulletin/2021/mar/developments-in-the-buy-now-pay-later-market.html>>.
- Kuhn K and X Vives (1995)**, 'Information Exchanges Among Firms and their Impact on Competition', Report for the European Commission, February.
- Occhiutto K (2020)**, 'The Cost of Card Payments for Merchants', RBA *Bulletin*, March, viewed 20 April 2021. Available at <<https://www.rba.gov.au/publications/bulletin/2020/mar/the-cost-of-card-payments-for-merchants.html>>.
- OECD (Organisation for Economic Co-operation and Development) (2001)**, 'Price Transparency', Roundtable on Competition Policy, 11 September.
- Productivity Commission (2018)**, 'Competition in the Australian Financial System', Inquiry Report No. 89, 29 June. Available at <<https://www.pc.gov.au/inquiries/completed/financial-system/report/financial-system-overview.pdf>>.
- RBA (Reserve Bank of Australia) (2019a)**, *The Operation of the Interchange Standards: Conclusions Paper*, May.
- RBA (2019b)**, *Review of Retail Payments Regulation: Issues Paper*, November. Available at <<https://www.rba.gov.au/payments-and-infrastructure/review-of-retail-payments-regulation/pdf/review-of-retail-payments-regulation-issues-paper-nov-2019.pdf>>.
- RBA (2021a), *Guidance for new issuers on certification under standard no. 1 of 2016 and standard no. 2 of 2016*, February. Available at <<https://www.rba.gov.au/payments-and-infrastructure/payments-system-regulation/pdf/guidance-certification-requirements-for-new-issuers.pdf>>.
- RBA (2021b)**, *Submission to the Review of the Australian Payments System*, January.

Stewart C, I Chan, C Ossolinski, D Halperin and P Ryan (2014), 'The Evolution of Payment Costs in Australia', RBA Research Discussion Paper No 14. Available at <<https://www.rba.gov.au/publications/rdp/2014/pdf/rdp2014-14.pdf>>.

Appendix A: Summary of Stakeholder Feedback

The Issues Paper noted some developments in the operation of card payment systems that have caused concern for various stakeholders and also for the Bank. The Bank invited views from interested parties, including both industry participants and end users, on possible policy responses. In total, more than 50 submissions were received from a wide range of financial institutions, merchants, card schemes, consumer groups and individuals; 38 of these have been published on the Bank's website, with the remaining submissions received in confidence. Around 25 parties took up the invitation to have discussions with the Bank, with a range of stakeholders also having follow-up meetings.

Strategic issues in the retail payments system

Many stakeholders raised the rapid pace of innovation in the payments system as a key strategic issue. A key concern was that many new players were largely unregulated, raising potential regulatory arbitrage and competitive neutrality concerns. Stakeholders were typically most concerned about the expansion of BNPL providers and the activities of large technology companies. Many stakeholders felt that these participants should be subject to the same rules as the incumbent payment providers.

Responses sometimes raised that regulation was too backward-looking and was slow to respond to emerging issues and new technologies. In particular, some stakeholders felt that regulation should play a greater role in ensuring standardisation and interoperability of payment technologies and platforms, and addressing 'technology lock-out'. This was raised especially in the context of online payments, tokenisation, QR codes and digital identity. At the same time, several stakeholders emphasised the importance of managing the decline of legacy payment methods such as cheques and cash.

Several stakeholders argued for greater industry coordination, particularly on a strategic vision for future systemic innovations and the management of domestic infrastructure; others highlighted the importance of access regimes to ensure fair and reasonable terms to connect to payments systems. Respondents also urged the Bank to ensure that it considered factors beyond cost when examining the efficiency of the payments system, including several suggestions to place greater emphasis on the security and resilience of the payments system.

Dual-network debit cards and least-cost routing

Many stakeholders expressed support for continued issuance of DNDCs. However issuers highlighted that there are significant costs associated with issuing DNDCs. Issuers noted there are limited cost synergies from operating two debit networks despite the similarities in their product offering. Issuers flagged there are cost duplications relating to investment spending, product upgrades and mandate compliance. The major banks argued it is more expensive for them to support multiple debit networks given their legacy systems. On the other hand, smaller issuers argued that the time and opportunity costs associated with issuing DNDCs hinders their ability to innovate and compete with the major banks. These extra costs can run into the millions of dollars, and small-to-medium sized issuers said they

account for a significant share of their total debit card spending and investment. Other stakeholders noted that eftpos has been supportive of small issuers in meeting their compliance mandates through financial support and flexibility in compliance deadlines.

Most issuers felt that having multiple networks on a debit card added little value to their customers. However, some smaller issuers with customer bases outside the large cities said their customers value eftpos' cash-out at point-of-sale functionality. Issuers that have begun the process of switching to SNDCs argued that SNDCs reduced the complexity of their product developments and would allow them to launch new product offerings (such as the mobile 'pays') for their customers more quickly. Some stakeholders also noted that the shift towards digital 'form factors' such as mobile wallets is making physical cards less important. The convenience of DNDCs for cardholders was said to be overemphasised, given that cardholders can now easily store multiple cards in their digital wallets. While issuers recognised the system-wide benefits of DNDCs, most issuers said that they would like the freedom to make a commercial decision about the issuance of DNDCs based on the needs of their customers, the costs involved and the value provided by each scheme. Several stakeholders noted that the financial case for large merchants to adopt LCR would be undermined if SNDCs became more prevalent, particularly given the growth of non-routable digital wallet transactions.

Most stakeholders were, in principle, supportive of LCR, although few supported making it a regulatory requirement. In the device-present environment, some stakeholders suggested a range of additional steps that the Bank could take to increase LCR adoption among merchants, including: mandating the provision of LCR on an 'opt-out' basis and requiring that all merchants be provided with 'dynamic' routing functionality which realised the full possible savings from LCR. In the online environment, stakeholders generally felt that the Bank should not mandate the provisioning of LCR. Some of the major banks noted that developing LCR functionality online would be costly, time consuming and potentially redundant if LCR is not relevant in the online checkout environment of the near future.

A number of stakeholders argued that there are material differences between the security and product offerings of the debit card schemes, particularly in the online context. Given the higher incidence of fraud in e-commerce transactions, some of these stakeholders argued that LCR online would increase fraud rates, adversely affecting all stakeholders in the online payments ecosystem. Accordingly, these stakeholders felt that customers should either be given an explicit choice of scheme or at least notified if their transaction was being routed. However, there was disagreement about the form the notification should take. A few stakeholders also argued that if customers were going to be notified of routing, there would need to be a degree of customer education. Other stakeholders had an opposing view, arguing that the schemes provide customers with comparable product offerings, and that there is (or soon will be) little difference between their security functionalities. These stakeholders also said that customers typically do not have a preferred debit schemes, and have a limited understanding of their debit options, so notifying them would only create confusion.

Nearly all stakeholders were opposed to any requirement to provide customers with an option to override a merchant's routing decision. Many stakeholders said that merchants are striving to create streamlined checkout experiences for customers online, and argued that an override option would add complexity and friction to the checkout process which would lead to more customers abandoning their purchase; accordingly, any requirement to provide an override option would lead to merchants avoiding LCR altogether. Some gateways noted that adding an override option would increase the technical complexity of building LCR online. Some banks also noted that LCR rules should be consistent in the device-present and online space as the boundaries between the two are blurring and will continue to do so in the future.

Competition in card acquiring

Many stakeholders noted that competition in the acquiring market is strong, pointing to a range of new entrants in recent years and declining acquirer margins. Innovation has increased the breadth of services available to merchants, and some stakeholders noted that technology-focused new entrants have been increasingly capturing market share from traditional (bank) acquirers. Some major banks argued that smaller players have been able to leverage existing payments infrastructure and face fewer compliance obligations (e.g. where a non-bank provider such as a payment facilitator offers acquiring services without becoming a fully licensed acquirer).

Nonetheless, several stakeholders noted that the acquiring market is still very concentrated, and that large bank acquirers have some key competitive advantages over smaller providers. These include the ability to 'bundle' acquiring services with broader business banking services, process 'on-us' transactions (where they are both the issuer and acquirer), and provide same-day settlement to merchants.

The Bank heard concerns from many stakeholders that issues regarding complexity and transparency can impede competition in the acquiring market. Many merchants struggle to understand the various cost components that make up their merchant service fees, while others who seek more information about these components may not be provided with the requested information. These issues tend to be exacerbated for smaller merchants, which often do not have the time or resources to investigate whether their pricing plan is competitive and, if not, to search for a better deal. On the other hand, one stakeholder noted that the relatively higher margins for smaller merchants may be driven by economic factors, for example related to smaller merchants having a higher risk profile.

On the whole, stakeholder feedback suggested that there is considerable inertia in merchants' choice of acquirers and pricing plans (although some large acquirers reported relatively high rates of switching in some market segments).

Scheme fees

There was widespread support among stakeholders for greater transparency of scheme fees. Several submissions noted that scheme fees are representing an increasing proportion of card payment costs, and that greater transparency could improve merchants' understanding of these costs and promote competition between the schemes. Some stakeholders suggested that smaller acquirers – which may pay higher scheme fees – could also benefit if greater competitive tension led to downward pressure on scheme fees.

While many submissions did not discuss the form greater transparency should take, suggestions included requiring acquirers to publish the average total scheme fees paid to each scheme or requiring schemes to publish their full fee schedules. One respondent suggested that disclosure would need to be sufficiently detailed to help merchants make more informed decisions on transaction routing for different transaction types.

The international schemes argued against scheme fee disclosure, primarily due to the commercial sensitivity of scheme fee schedules. One scheme also questioned the usefulness of scheme fee transparency for smaller merchants (who preferred simplicity and were largely focused on the overall cost of their payments), while another scheme argued that such disclosure would put regulated card schemes at a competitive disadvantage to other schemes.

Regardless of whether they supported scheme fee transparency, most respondents noted the complexity of these fees and the difficulty of ensuring that disclosures would be meaningful to merchants. Several issuers and acquirers said that it would be difficult for them to report accurate information on scheme fees for specific types of card transactions, and that the Bank would need to ensure that any assumptions and methodologies used for reporting such data were consistent across reporting institutions.

Access regimes

Stakeholders largely agreed that the arrangements around access regimes have been generally working well. Although occasionally a party may have experienced some delays when getting access, no responses proposed significant changes to existing policies.

Digital wallets and mobile payment applications

A number of stakeholders noted that the entry of large multinational technology companies could pose challenges for the local market. Providers of digital wallets and other mobile payments services are often very large, and even the largest domestic participants in the Australian payments system (such as the major banks) may find themselves in a weak negotiating position when partnering with them.

Some stakeholders argued that certain practices of digital wallet providers may be detrimental for competition and introduce new costs into the payments system. In particular, some issuers expressed concerns about the ability of digital wallet providers to restrict access to the underlying technology used for contactless mobile payments (such as NFC) and prohibit issuers from passing on digital wallet fees to customers. One issuer also noted that issuers may be required to share some aspects of consumers' card transaction data with one of the digital wallet providers. Another stakeholder highlighted the lack of transparency related to digital wallet fees, which, although not directly borne by consumers or merchants, represent a new input cost in the payments ecosystem.

Other stakeholders noted the benefits of digital wallets, including their convenience and potential to improve security through technologies such as tokenisation and biometric authentication. One stakeholder argued that broadening third-party access to NFC infrastructure in mobile devices could compromise the security and privacy of digital wallet transactions.

Finally, some feedback noted that not all digital wallet providers support dual-network functionality for dual-network debit cards provisioned in their wallets. In addition, it was noted that issuer support for dual-network functionality can also be required for the functionality to be available to customers; for example, this may involve the issuer enabling the tokenisation services for both schemes.

Interchange fees

There was limited support for a further lowering of the interchange benchmarks, with many stakeholders noting that Australian interchange fees are already low by international standards. Many stakeholders argued that interchange revenue is essential to support continued investment in innovation, security and the provision of services by card issuers. There were some concerns about a reduction in the debit interchange cap, with stakeholders expecting that this would lead to a corresponding fall in weighted-average interchange rates and limit the schemes' ability to use their interchange schedules to incentivise innovation and the adoption of certain functionality. It was also noted that smaller issuers would be disproportionately disadvantaged by any further interchange reductions as they have fewer other

sources of revenue to offset this, which could undermine their ability to compete; indeed, some issuers claimed that they were making a loss on many transactions due to the low interchange fees paid by strategic merchants. Relatedly, two issuers proposed a floor on interchange fees to reduce the difference between interchange paid by large and small merchants and provide certainty of income to card issuers. Some stakeholders also argued that merchants' right to surcharge provides sufficient competitive pressure on payment costs, and that the new interchange standards have only been in effect for a few years so it was too early to consider making any further changes.

In contrast, some merchant and consumer groups argued for a further lowering of the benchmarks to place downward pressure on card acceptance costs. Some stakeholders also pointed out that the cents-based cap on debit transactions has allowed schemes to set unreasonably high interchange rates (in percentage terms) on some low-value transactions. There were also concerns that the wide range of interchange fees has disproportionately benefited larger merchants by enabling them to negotiate discounted rates; these discounts have caused schemes to raise the 'standard' interchange rates paid by smaller merchants to maintain a high overall level of interchange fees for issuers.

Regarding the operation of the interchange standards, some stakeholders commented that the current quarterly compliance cycle for interchange benchmarks had increased the frequency of interchange resets by the schemes, which imposed significant costs on participants in the payments system.

There were mixed views on whether to extend the interchange regulation to three-party schemes and transactions on foreign-issued cards. Those in favour generally cited the relatively higher costs of these payment methods and the principle of competitive neutrality. In contrast, arguments against applying interchange regulation to the three-party schemes included that: competitive pressures have seen merchant fees fall at least as much as those on four-party schemes since interchange regulation was introduced; three-party schemes have not increased their overall market share over the past few decades; and merchants can surcharge three-party cards or choose not to accept them as they are generally seen as optional for both merchants and customers. There was also little indication of what form regulation of three-party schemes might take. Arguments against extending interchange regulation to foreign-issued cards included: the continued limited use of such cards in Australia; the international schemes having rules that prevent circumvention of domestic interchange caps by issuance of foreign cards; the unfair advantage it would confer on unregulated international schemes; and uncertainty about the eventual impact of the EU's recent move to reduce interchange on foreign-issued cards. The international schemes also highlighted that cross-border transactions have unique risks and complexities (including higher fraud rates) that increase issuer costs and justify higher interchange rates.

Net compensation

Schemes and issuers generally indicated that the current net compensation provisions were working effectively, although some suggested they were complex and difficult to interpret. Some noted small changes that might be beneficial. For example, some stakeholders suggested that aspects of the provisions may hinder competition between schemes (e.g. requiring payments for card portfolio conversions to be included as issuer receipts may give incumbent schemes an advantage, and the move from cash to accruals may favour international schemes that pay large upfront incentives). Others felt that the burden of monitoring compliance primarily fell on issuers, not schemes, and recommended that substantive obligations should also apply to schemes. While parties generally agreed that there needed to be close monitoring to dissuade and detect potential circumvention, few saw a case to develop new enforcement mechanisms to strengthen observance of the provisions.

Surcharging

Stakeholders were generally of the view that the revised surcharging framework put in place following the 2015-16 Review was functioning well. Merchants, consumer groups and banks generally supported merchants' right to apply a surcharge on more expensive payment methods. International card schemes repeated their long-held view that surcharging should not be permitted, including because merchants benefit from accepting electronic payment methods and payment costs are now at a level where merchants should not need to surcharge.

While the framework was generally viewed as functioning well overall, a few possible shortcomings were raised. These included: some merchants may be surcharging above the cost of acceptance; some industries were exempt from the regulation (such as the taxi industry); and that tokenisation may affect merchants' ability to identify card types, preventing them from being able to apply an appropriate surcharge. It was also observed that if a merchant was on a blended (or bundled) plan, it may be difficult to closely relate surcharges to the underlying costs of different payment methods.

In relation to the no-surcharge rules imposed by BNPL schemes, a number of merchant stakeholders were of the view that it was essential for merchants to accept BNPL for competitive reasons, particularly for certain types of transactions (e.g. online retail payments). Some stakeholders also noted that the fees charged to merchants for BNPL transactions can be high compared to the cost of accepting other electronic payment methods, yet merchants are unable to apply a surcharge to recoup the cost of accepting BNPL payments. Banks, merchants and consumer groups were generally in favour of requiring BNPL providers to remove their no-surcharge rules, largely on the basis of these higher costs, consistency and competitive neutrality.

In contrast, BNPL providers were of the view that there was not a case for removing no-surcharge rules, arguing that the industry is still emerging, is a competitive part of the retail payments landscape, and remains small relative to the size of other electronic payment methods. A number of BNPL providers also argued that some BNPL products provide a range of services to merchants including marketing and customer referrals, not just payments processing and that it would not be appropriate for merchants to be able to pass on the full cost of offering BNPL to consumers. Some stakeholders also were of the view that if merchants were to levy a surcharge on consumers who use BNPL, it could result in the BNPL provider no longer qualifying for certain credit regulation exemptions.

In terms of the effect of competition on merchant costs, stakeholder views were mixed on whether competition between providers was resulting in lower BNPL merchant fees. Whereas some stakeholders observed that the entry of new providers was leading to increased price competition, others noted that it could be difficult for merchants to stop accepting payments from certain BNPL providers.

Regulation and enforcement

Stakeholders generally did not raise any significant suggestions for changing the Bank's regulatory powers or enforcement mechanisms, although there was some level of support for giving the Bank greater powers to correct non-compliance. Stakeholders did, however, have some suggestions for changing the Bank's regulatory approach to make it more responsive, flexible and future-proof. For example, there were various suggestions that the Bank should speed up its regulation-making processes and adopt a more activities-based and product/technology-neutral approach to regulation that is better able to adapt to changes in the market and support a level playing field.

Appendix B: Draft Standards

DRAFT STANDARD NO. 1 OF 2016

THE SETTING OF INTERCHANGE FEES IN THE DESIGNATED CREDIT CARD SCHEMES AND NET PAYMENTS TO ISSUERS

1. Objective

The objective of this Standard is to ensure that the setting of interchange fees and payments and other transfers of valuable consideration having an equivalent object or effect to interchange fees in each designated credit card scheme is transparent and promotes:

- *efficiency; and*
- *competition*

in the Australian payments system.

2. Application

2.1 This Standard is determined under Section 18 of the *Payment Systems (Regulation) Act 1998* (the **Act**).

2.2 This Standard applies to each of the following, each of which is referred to in this Standard as a **Scheme**:

(a) the payment system operated within Australia known as the MasterCard system which was designated under the Act as a payment system on 12 April 2001 and which is referred to in this Standard as the **MasterCard System**; and

(b) the payment system operated within Australia known as the VISA system, which was designated under the Act as a payment system on 12 April 2001 and which is referred to in this Standard as the **VISA System**; and.

~~(c) the American Express Companion Card payment system operated within Australia, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as the **American Express Companion Card Scheme**.~~

2.3 In this Standard:

Above Benchmark Reference Period has the meaning given to it in clause 4.2;

Acquired includes accepted;

Acquirer means a participant in a Scheme in Australia that:

(a) provides services, directly or indirectly, to a Merchant to allow that Merchant to accept a Credit Card of that Scheme; or

- (b) is a Merchant that accepts, or is a Related Body Corporate of a Merchant that accepts, a Credit Card of that Scheme and bears risk as principal in relation to the payment obligations of the Issuer of that Credit Card in relation to that acceptance;

Associated Entity has the meaning given by Section 50AAA of the *Corporations Act 2001*;

Benefit means:

- (a) a payment, receipt, rebate, refund or allowance;
- (b) in relation to any Property or service received or receivable by a Direct Issuer Participant:
 - (i) where there is a Regular Price for that Property or service, any discount or deduction from that price;
 - (ii) where there is not a Regular Price for that Property or service, an amount by which the Fair Value of the Property or service exceeds the payment or other similar financial consideration made or given for it by the Direct Issuer Participant; and
- (c) a benefit (however named or described) of a similar nature to, or having the same effect as, a benefit of the kind specified in (a) or (b) above;

Commencement Date means 1 July 2017;

Core Service means, in relation to a Scheme, a service provided by the administrator of the Scheme in Australia or any of its Associated Entities that meets the requirements in the following paragraphs (a), (b) and (c):

- (a) the service is used by a participant in the Scheme in Australia in relation to Devices of the Scheme that can be used for purchasing goods or services on credit or transactions initiated using those Devices; and
- (b) without the service it would not be possible for a Direct Issuer Participant to be an Issuer or for another entity to be an Issuer through Sponsorship by a Direct Issuer Participant of the Scheme; and
- (c) the service (however named or described) relates to one or more of the following (each a Core Function) and only to one or more Core Functions:
 - (i) the licensing of the Scheme's brands and other intellectual property owned by, or licensed to, the administrator of the Scheme in Australia or any of its Associated Entities, a licence (or sub-licence) of which is required in order to be a participant in the Scheme;
 - (ii) connection to, and/or maintenance of a connection to, the systems to which it is necessary to connect in order to be a participant in the Scheme;
 - (iii) transaction processing (including processing of charge-back transactions);
 - (iv) clearing and settlement (including clearing and settlement of charge-back transactions);
 - (v) authentication;
 - (vi) authorisation;
 - (vii) stand-in processing, clearing and settlement;
 - (viii) fraud prevention; and

- (ix) handling, investigating and settling disputes, and requests or claims for chargebacks, raised by holders of Devices.

A service will relate only to one or more Core Functions for the purpose of this paragraph (c) even if it involves or includes incidental services necessary to support one or more Core Functions;

Credit Card Account means, in relation to a Credit Card of a Scheme, the account that is debited when that Device is used to purchase goods or services on credit;

Credit Card of a Scheme or **Credit Card of that Scheme** means, in relation to a Scheme, a Device issued by a participant in the Scheme in Australia under the Rules of the Scheme that can be used for purchasing goods or services on credit;

Credit Card Transaction means, in relation to a Scheme, a transaction in that Scheme between a holder of a Credit Card of that Scheme and a Merchant involving the purchase of goods or services using a Credit Card of that Scheme that is Acquired by an Acquirer (but does not include any transaction to reverse such a transaction or provide a credit or make a chargeback in relation to such a transaction);

Debit Card Scheme means each payment system referred to as a 'Scheme' under *Standard No. 2 of 2016 The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers*;

Device means any card, plate or other payment code or device, including a code or device where no physical card or other embodiment is issued and a code or device used or to be used for only one transaction;

Direct Issuer Participant means, in relation to a Scheme, a participant in that Scheme in Australia as an Issuer, or as a Sponsor for one or more Issuers, that is not an Indirect Issuer Participant in that Scheme in Australia. Without limitation, for the:

- (a) MasterCard System this means any Principal Customer or Association Customer, each as defined in the Rules of the Scheme, in its capacity as Issuer or as Sponsor for one or more Issuers; or
- (b) VISA System this means any Principal-Type Member as defined in the Rules of the Scheme in its capacity as Issuer or as Sponsor for one or more Issuers;

Direct Issuer Participant Payments has the meaning given to it in clause 5.2;

Direct Issuer Participant Receipts has the meaning given to it in clause 5.2;

Fair Value means, in relation to any Property or service:

- (a) subject to paragraph (b), the amount that would be paid to acquire the Property or service in an orderly transaction between independent, unrelated and well informed parties at the earlier of:
 - (i) the date the Property or service was first provided; and
 - (ii) the date the Property or service was committed to be provided,to the Direct Issuer Participant; but
- (b) if at any subsequent time the amount that would be paid to acquire the Property or service in an orderly transaction between independent, unrelated and well informed parties (**Revised Value**) is materially different from the amount determined in accordance with paragraph (a) (or, if any adjustment is made in accordance with this

paragraph (b), the most recent such adjustment), the Fair Value may be adjusted to that Revised Value provided:

- (i) use of that Revised Value as Fair Value is fair and reasonable and consistent with the objective of this Standard; and
- (ii) the Fair Value may be adjusted to a Revised Value no more than once in a Reporting Period;

Incentive Test: a Benefit meets the **Incentive Test** in relation to a Scheme if it is given for a purpose of, or has or will likely have the effect of, any one or more of the following:

- (a) incentivising the entry into of a contract relating to the issue of Credit Cards of the Scheme;
- (b) promoting or incentivising the issuance or use of Credit Cards of the Scheme; or
- (c) providing or funding incentives to holders of Credit Cards of the Scheme to use those cards.

Benefits that meet the Incentive Test in relation to a Scheme include lump-sum, volume based and transaction-specific Benefits such as:

- (i) incentives to market Credit Cards of the Scheme; and
- (ii) any of the following earned, accrued or receivable by a Direct Issuer Participant for agreeing to issue Credit Cards of the Scheme or for Credit Card Transactions undertaken in the Scheme meeting or exceeding a specific transaction volume, percentage share or dollar amount of transactions processed:
 - (A) a rebate on any fees or other costs or charges, whether for a Core Service or for any other product or service;
 - (B) a discount from the Regular Price of any Property or service, whether the Property or service is related to Credit Cards of the Scheme or not;

Indirect Issuer Participant means, in relation to a Scheme, a participant in that Scheme in Australia as an Issuer that participates in the Scheme in Australia as Issuer through the Sponsorship of another participant in that Scheme. Without limitation, for the:

- (a) MasterCard System this means any Affiliate Customer as defined in the Rules of the Scheme in its capacity as Issuer; or
- (b) VISA System this means any Participant-Type Member or Associate-Type Member, each as defined in the Rules of the Scheme, in its capacity as Issuer;

Initial Reporting Period means, in relation to a New Issuer, the period commencing on the first date on which any Direct Issuer Participant Payments or Direct Issuer Participant Receipts were paid, became payable, were earned or accrued, or became receivable by or to the New Issuer (as applicable) and ending on the last day of the first full financial year following Public Launch by that New Issuer;

Interchange Fee Category has the meaning given to it in clause 4.1(b);

Interchange Fees means:

~~(, in relation to a) — for each of the VISA System and the MasterCard System Scheme, wholesale fees, known as interchange fees, which are payable between an Issuer and an Acquirer, directly or indirectly, in relation to Credit Card Transactions in the Scheme; and;~~

~~(b) — for the American Express Companion Card Scheme, wholesale fees, known as issuer fees or issuer rates, which are payable, directly or indirectly, between an Issuer which is a participant in the Scheme in Australia and the Acquirer or an administrator of the Scheme in Australia, or any Related Body Corporate of either of them, and any other Credit Card Transaction-based payments which are functionally equivalent to such issuer fees or issuer rates or to the fees described in paragraph (a) above;~~

International Card Transaction means, in relation to a Scheme, a transaction in that Scheme that:

(a) is between a holder of a Device issued by an International Issuer and a merchant in Australia;

(b) involves the purchase of goods or services; and

(c) is Acquired by an Acquirer,

but does not include any transaction to reverse such a transaction or provide a credit or make a chargeback in relation to such a transaction;

International Interchange Fee means, in relation to a Scheme, wholesale fees, known as interchange fees, which are payable between an International Issuer and an Acquirer, directly or indirectly, in relation to International Card Transactions in the Scheme;

International Interchange Fee Category means a category of International Card Transactions in relation to which a particular International Interchange Fee applies, which may be:

(a) determined by reference to the nature of the holder or type of the Device, the identity or nature of the merchant, the means of effecting the transaction, the security or authentication that applies or any other matters; or

(b) a residual category covering transactions not in any other category;

International Issuer means a participant in a Scheme that has a contractual relationship with its customers under which it issues Devices of the Scheme to those customers or their nominees but that is not an Issuer;

International Multilateral Interchange Fee means, in relation to a Scheme, an International Interchange Fee that is determined by an administrator of the Scheme or any of its Associated Entities and applies regardless of the identity of the Acquirer or International Issuer paying or receiving the International Interchange Fee;

Issuer means a participant in a Scheme in Australia that has a contractual relationship with its customers under which it issues Credit Cards of a Scheme to those customers or their nominees;

Merchant means, in relation to a Scheme, a merchant in Australia that accepts a Credit Card of that Scheme for payment for goods or services;

Multilateral Interchange Fee means, in relation to a Scheme, an Interchange Fee that is determined by an administrator of the Scheme and applies regardless of the identity of the Acquirer or Issuer paying or receiving the Interchange Fee;

Net Compensation has the meaning given to it in clause 5.1;

New Issuer means a Direct Issuer Participant in a Scheme that has not, before commencing the issue of any Cards of that Scheme, issued in Australia any Devices of any other Scheme or any Debit Card Scheme;

Public Launch in relation to a New Issuer, occurs when the New Issuer begins offering to issue Cards of a Scheme to its intended customer base and will not be taken to have occurred when a New Issuer has only issued Cards of that Scheme to its staff or a select group of its customers or other persons as part of a trial or test phase;

Property means any property including any good and any proprietary right or interest;

Quarter means a 3 month period ending on 30 June, 30 September, 31 December or 31 March;

Reference Period means a 12 month period ending on the last day of a Quarter;

Regular Price means, in relation to Property or a service, a supplier and a Direct Issuer Participant at any time, the price at which the supplier is regularly supplying Property or services of the same description to entities of a class, group or type that includes the Direct Issuer Participant at that time;

Related Body Corporate has the meaning given in the *Corporations Act 2001*;

Relevant Portion has the meaning given to it in clause 5.2;

Reporting Period means a 12 month period ending 30 June;

Rules of a Scheme or **Rules of the Scheme** means the constitution, rules, by-laws, procedures and instruments of the relevant Scheme as applied in Australia, and any other arrangement relating to the Scheme by which participants in that Scheme in Australia are, or consider themselves to be, bound;

Sponsor means a participant in a Scheme in Australia who has accepted responsibility in whole or in part for, or to act as agent for, another entity under and in accordance with the Rules of the Scheme so that the other entity may participate in the Scheme and **Sponsorship** has a corresponding meaning;

include or **including** or **such as** when introducing an example do not limit the meaning of the words to which the example relates to that example or examples of a similar kind; and terms defined in the Act have the same meaning in this Standard.

2.4 For the purposes of this Standard:

- (a) a provision of a plan, arrangement or agreement shall be deemed to have a particular purpose if the provision was included in the plan, arrangement or agreement by a party or parties for purposes that include that purpose and that purpose was a substantial purpose; and
- (b) conduct including the payment or receipt of a fee or the giving of a benefit or other valuable consideration shall be deemed to have been made for a particular purpose if the person undertaking the conduct, payment or receipt did so for purposes that include that purpose and that purpose was a substantial purpose.

2.5 Each participant in a Scheme must do all things necessary on its part to ensure compliance with this Standard.

2.6 If any part of this Standard is invalid, this Standard is ineffective only to the extent of such part without invalidating the remaining parts of this Standard.

2.7 This Standard is to be interpreted:

- (a) in accordance with its objective; and

(b) by looking beyond form to substance.

2.8 For the purposes of this Standard, an Interchange Fee paid from an Acquirer to an Issuer is to be expressed as a positive number and an Interchange Fee paid from an Issuer to an Acquirer is to be expressed as a negative number.

2.9 On the Commencement Date this Standard replaces *Standard No. 1, The Setting of Wholesale (Interchange) Fees in the Designated Credit Card Schemes* relating to each of the VISA System and MasterCard System. Neither the registration nor the terms of this Standard affect that standard before the Commencement Date.

3. Anti-Avoidance

A participant in a Scheme must not, either alone or together with one or more other persons, enter into, begin to carry out or carry out a plan or arrangement or otherwise be knowingly involved in a plan or arrangement if it would be concluded that the person did so for a purpose of avoiding the application of this Standard, and the plan or arrangement or part of the plan or arrangement has achieved or would but for this provision have achieved or could reasonably be considered to have achieved that purpose.

4. Interchange Fees

4.1 (a) An Interchange Fee (exclusive of goods and services tax) in relation to a Credit Card Transaction must not exceed 0.800 per cent of the value of the Credit Card Transaction to which it relates.

(b) If an Interchange Fee applies in relation to a category of Credit Card Transactions (whether that category is determined by reference to the nature of the holder, or type, of the Credit Card of the Scheme, the identity or nature of the Merchant, the means of effecting the transaction, the security or authentication that applies or any other matter, or is a residual category covering transactions not in any other category) (**Interchange Fee Category**), that Interchange Fee must be:

(i) a percentage of the value of the Credit Card Transaction to which it relates; or

(ii) a fixed amount,

applying to all Credit Card Transactions in the category, and cannot be expressed as a range of rates or amounts.

4.2 If the total value of Interchange Fees (exclusive of goods and services tax) payable in relation to Credit Card Transactions undertaken in a Scheme during a Reference Period exceeds 0.500 per cent of the total value of those Credit Card Transactions:

(a) that Reference Period will be an **Above Benchmark Reference Period**; and

(b) the participants in that Scheme must take all necessary steps to vary the rates or amounts of Interchange Fees applicable under that Scheme, with effect no later than 2 months and 1 day after the end of the Above Benchmark Reference Period, to rates or amounts such that, had those varied rates or amounts applied under the Scheme during that Above Benchmark Reference Period, that Reference Period would not have been an Above Benchmark Reference Period.

4.3 If at any time any Interchange Fee applicable under a Scheme is introduced or removed, or the rate or amount of any Interchange Fee under a Scheme is varied, the Interchange Fees applicable under that Scheme following that change must be such that, had they

applied for the whole of the most recent Reference Period prior to the date of the change, that Reference Period would not have been an Above Benchmark Reference Period. Nothing in this clause 4.3 limits clause 4.2.

5. Net Payments to Direct Issuer Participants

5.1 ~~No~~Subject to clause 6.5, no Direct Issuer Participant in a Scheme may receive, directly or indirectly, Net Compensation in relation to Credit Card Transactions undertaken in that Scheme. **Net Compensation** is received by a Direct Issuer Participant if the Direct Issuer Participant Receipts of the Direct Issuer Participant for that Scheme in respect of a Reporting Period exceed the Direct Issuer Participant Payments of the Direct Issuer Participant for that Scheme in respect of that Reporting Period.

5.2 For the purpose of this clause 5:

- (a) subject to paragraphs (c), (d), (e), (f) and (g), **Direct Issuer Participant Receipts** of the Direct Issuer Participant for a Scheme and a Reporting Period is the total of the Benefits that meet the Incentive Test in relation to the Scheme that are earned or accrued during, or receivable in respect of, the Reporting Period by the Direct Issuer Participant and payable, allowable or otherwise to be provided, directly or indirectly, by the administrator of the Scheme in Australia or any of its Associated Entities but, if such an Associated Entity is an Acquirer, excluding Interchange Fees;
- (b) subject to paragraphs (c), (d), (e), (f) and (g), **Direct Issuer Participant Payments** of the Direct Issuer Participant for a Scheme and a Reporting Period is the total amount paid or payable, directly or indirectly, by the Direct Issuer Participant to or in favour of the administrator of the Scheme in Australia or any of its Associated Entities in relation to Core Services provided during or in respect of the Reporting Period for Credit Cards of the Scheme or Credit Card Transactions undertaken in the Scheme;
- (c) if a Benefit referred to in paragraph (a) or (b) does not relate solely to Credit Cards of the Scheme or Credit Card Transactions undertaken in the Scheme and also relates to other Devices or other transactions:
 - (i) the Benefit must be apportioned between:
 - (A) the Credit Cards of the Scheme and Credit Card Transactions on the one hand; and
 - (B) the other Devices and other transactions on the other, fairly and reasonably, having regard to, where relevant, the transaction history on Devices used in the payment systems to which the Benefit relates and the proportion of the Devices to which the Benefit relates that are Credit Cards of the Scheme issued by the Direct Issuer Participant or by any Indirect Issuer Participant through Sponsorship by that Direct Issuer Participant; and
 - (ii) the portion referable to Credit Cards of the Scheme and Credit Card Transactions determined in accordance with sub-paragraph (i) (the **Relevant Portion**) must be included in the determination of Direct Issuer Participant Receipts or Direct Issuer Participant Payments, as applicable;
- (d) one method of apportionment under clause 5.2(c) that will be fair and reasonable for the purpose of that provision is an apportionment on a pro-rata basis, based on the value of Credit Card Transactions undertaken in the Scheme using Credit Cards of the Scheme during the Reporting Period as a proportion of the total value of the

transactions undertaken in any payment system to which the Benefit relates during the Reporting Period. This does not preclude an apportionment in another way that meets the requirements of clause 5.2(c);

(e) where a Benefit referred to in paragraph (a), (b) or (c) relates to a period that spans more than one Reporting Period, the Benefit or, in the case of a Benefit referred to in paragraph (c), the Relevant Portion of the Benefit, may be allocated among Reporting Periods, in which case the allocation must:

- (i) be on a pro-rata basis based on the number of months in each relevant Reporting Period to which the Benefit relates if an allocation on that basis would fairly and reasonably align the Benefit to the activity to which the Benefit relates; or
- (ii) otherwise on some other basis that fairly and reasonably aligns the allocation of the Benefit to the activity to which the Benefit relates,

in each case provided that:

- (iii) no part of it is allocated to any Reporting Period the whole of which occurs before the term of the contract or arrangement under which the Benefit is payable, receivable or allowable has commenced;
- (iv) no part of it is allocated to any Reporting Period the whole of which occurs after the term of the contract or arrangement under which the Benefit is payable, receivable or allowable has ended; and
- (v) it may not be allocated among more than 10 consecutive Reporting Periods;

(f) a Direct Issuer Participant who adopts a particular method permitted by clause 5.2 of this Standard of:

- (i) determining whether and to what extent:
 - (A) Benefits are earned or accrued during, or are receivable in respect of, a Reporting Period for the purposes of paragraph 5.2(a); or
 - (B) Core Services are provided during or in respect of a Reporting Period for the purposes of paragraph 5.2(b); or

(ii) allocating or apportioning Benefits for the purpose of paragraph (c), (d) or (e), must, unless the Reserve Bank of Australia otherwise agrees in writing, continue to use the same method consistently from one Reporting Period to the next; and

(g) for the purpose of this clause 5, a Direct Issuer Participant must ensure that:

- (i) a Benefit paid, allowed or otherwise provided, directly or indirectly, by the administrator of the Scheme in Australia or any of its Associated Entities that meets the Incentive Test is included as a Direct Issuer Participant Receipt in the calculation of Net Compensation in respect of a Reporting Period; and
- (ii) an amount treated as a Direct Issuer Participant Payment in the calculation of Net Compensation in respect of a Reporting Period is not included as a Direct Issuer Participant Payment in the calculation of Net Compensation for any other Reporting Period.

6. Reporting and Transparency

6.1 An administrator of a Scheme in Australia or a representative of the participants in the Scheme in Australia must publish [on the Scheme's website:](#)

(a) the Multilateral Interchange Fee rates or amounts (whichever is applicable) of the Scheme in Australia on the Scheme's website, including the rates or amounts for each Interchange Fee Category; and

(b) the International Multilateral Interchange Fee rates or amounts (whichever is applicable) of the Scheme, including the rates or amounts for each International Interchange Fee Category.

6.2 Each:

(a) Acquirer; and

(b) Issuer that is a Direct Issuer Participant,

that is a party to an agreement with one or more other participants in a Scheme to pay or receive Interchange Fees in relation to Credit Card Transactions in the Scheme that are not Multilateral Interchange Fees must report to the Reserve Bank of Australia by 31 July each year the range of Interchange Fee rates or amounts (whichever is applicable) it received or paid in respect of the most recent Reporting Period. The Reserve Bank of Australia may publish the reported range of these Interchange Fees for the Scheme on its website.

6.3 An administrator of a Scheme in Australia or a representative of the participants in the Scheme in Australia must on or before 31 July each year certify in writing to the Reserve Bank of Australia in respect of the most recent Reporting Period, that Interchange Fees of the Scheme in Australia were during that Reporting Period in compliance with this Standard.

6.4 Each Subject to clause 6.5, each of an administrator of a Scheme in Australia and each Direct Issuer Participant in the Scheme in Australia must on or before 31 July each year certify in writing to the Reserve Bank of Australia that it was, in respect of the most recent Reporting Period, in compliance with clause 5.

6.5.5 Where a Direct Issuer Participant in a Scheme is a New Issuer, each of the administrator of the Scheme in Australia and the New Issuer will be taken to have complied with its obligations under clause 5 and clause 6.4 in respect of the period prior to and including the Initial Reporting Period if it:

(a) complies with clause 5 as if each reference to 'Reporting Period' is read as a reference to the Initial Reporting Period; and

(b) certifies in writing to the Reserve Bank of Australia that it was, in respect of the Initial Reporting Period, in compliance with clause 5 read as specified in clause 6.5(a) and provides such certification on or before 31 July in the year that the Initial Reporting Period ends.

6.6 An administrator of a Scheme in Australia or a representative of the participants of the Scheme in Australia must, not later than 30 days after the end of each Quarter, certify in writing to the Reserve Bank of Australia each of the following for that Quarter for the Scheme:

(a) the total value of Credit Card Transactions undertaken in the Scheme in that Quarter;

(b) the number of Credit Card Transactions undertaken in the Scheme in that Quarter;

- (c) the total value of all Interchange Fees (exclusive of goods and services tax) payable in respect of the Credit Card Transactions undertaken in the Scheme during that Quarter;
- (d) the total value of Interchange Fees (exclusive of goods and services tax) payable in respect of Credit Card Transactions undertaken in the Scheme during the Quarter divided by the total value of the Credit Card Transactions undertaken in the Scheme during the Quarter; and
- (e) each Interchange Fee Category that applied for some or all of the Quarter and, for each of those categories:
 - (i) the Interchange Fee rates or amounts (whichever is applicable) that applied during the Quarter (expressed as a percentage or an amount, not as a range); and
 - (ii) the total value of Interchange Fees (exclusive of goods and services tax) payable in respect of that Quarter that are referable to Credit Card Transactions undertaken in the Scheme in that Quarter in that category.

7. Commencement and Implementation

- 7.1 This Standard came into force on the Commencement Date, but certain provisions in it had a transitional application as set out in clause 7 of this Standard as at the Commencement Date.
- 7.2 This Standard as varied with effect from 1 July 2019 must be complied with for the Reporting Period ending on 30 June 2020 and all subsequent Reporting Periods. For the Reporting Period ending on 30 June 2019 a Direct Issuer Participant in a Scheme may elect to comply, in relation to that Scheme, with either:
- (a) this Standard as in effect on 30 June 2019; or
 - (b) this Standard as amended with effect on 1 July 2019 as if this Standard so amended had been in effect from 1 July 2018,
- and must notify its election of (a) or (b) (**Transitional Election**) to the administrator of the Scheme no later than 1 July 2019.
- 7.3 An administrator of a Scheme in Australia that receives a notification under clause 7.2 from a Direct Issuer Participant must provide its certification of its compliance under clause 6.4 as that compliance relates to that Direct Issuer Participant and the Reporting Period ending on 30 June 2019 on the same basis as that specified in the Transitional Election made by that Direct Issuer Participant.
- 7.4 If a Direct Issuer Participant in a Scheme does not give a Transitional Election in accordance with clause 7.2 then:
- (a) it is taken to have elected to comply, in relation to that Scheme, with this Standard as in effect on 30 June 2019; and
 - (b) the administrator of the Scheme in Australia must provide its certification under clause 6.4 in relation to that Direct Issuer Participant and the Reporting Period ending on 30 June 2019 accordingly.

DRAFT STANDARD NO. 2 OF 2016

THE SETTING OF INTERCHANGE FEES IN THE DESIGNATED DEBIT AND PREPAID CARD SCHEMES AND NET PAYMENTS TO ISSUERS

1. Objective

The objective of this Standard is to ensure that the setting of interchange fees and payments and other transfers of valuable consideration having an equivalent object or effect to interchange fees in each designated debit card scheme and prepaid card scheme is transparent and promotes:

- *efficiency; and*
- *competition*

in the Australian payments system.

2. Application

2.1 This Standard is determined under Section 18 of the *Payment Systems (Regulation) Act 1998* (the **Act**).

2.2 This Standard applies to each of the following, each of which is referred to in this Standard as a **Scheme**:

- (a) the payment system operated within Australia known as Visa Debit, which was designated under the Act as a payment system on 23 February 2004 and which is referred to in this Standard as **Visa Debit**;
- (b) the payment system operated within Australia known as Visa Prepaid, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as **Visa Prepaid**;
- (c) the payment system operated within Australia known as Debit MasterCard, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as **Debit MasterCard**;
- (d) the payment system operated within Australia known as MasterCard Prepaid, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as **MasterCard Prepaid**;
- (e) the debit card payment system operated within Australia known as the EFTPOS payment system, which was designated under the Act as a payment system on 12 June 2012 and which is referred to in this standard as the **EFTPOS System**; and
- (f) the prepaid card payment system operated within Australia under the EFTPOS Scheme Rules, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this standard as **EFTPOS Prepaid**.

2.3 In this Standard:

Above Benchmark Reference Period has the meaning given to it in clause 4.2;

Acquired includes accepted;

Acquirer means a participant in a Scheme in Australia that:

- (a) provides services, directly or indirectly, to a Merchant to allow that Merchant to accept a Card of that Scheme; or
- (b) is a Merchant that accepts, or is a Related Body Corporate of a Merchant that accepts, a Card of that Scheme and bears risk as principal in relation to the payment obligations of the Issuer of that Card in relation to that acceptance;

Associated Entity has the meaning given by Section 50AAA of the *Corporations Act 2001*;

Benefit means:

- (a) a payment, receipt, rebate, refund or allowance;
- (b) in relation to any Property or service received or receivable by a Direct Issuer Participant:
 - (i) where there is a Regular Price for that Property or service, any discount or deduction from that price;
 - (ii) where there is not a Regular Price for that Property or service, an amount by which the Fair Value of the Property or service exceeds the payment or other similar financial consideration made or given for it by the Direct Issuer Participant; and
- (c) a benefit (however named or described) of a similar nature to, or having the same effect as, a benefit of the kind specified in (a) or (b) above;

Card Account means, in relation to a Card of a Scheme, the account that is debited when that Device is used to purchase goods or services;

Card of a Scheme or **Card of that Scheme** means a Debit Card of a Scheme or a Prepaid Card of a Scheme;

Card of a Scheme Pair means a Card of a Scheme that is part of a Scheme Pair;

Card Transaction means a Debit Card Transaction or a Prepaid Card Transaction;

Commencement Date means 1 July 2017;

Core Service means, in relation to a Scheme, a service provided by the administrator of the Scheme in Australia or any of its Associated Entities that meets the requirements in the following paragraphs (a), (b) and (c):

- (a) the service is used by a participant in the Scheme in Australia in relation to Devices of the Scheme that can be used to make payments for goods or services by:
 - (i) accessing a deposit account held at an authorised deposit-taking institution or a bank or other financial institution; or
 - (ii) using a store of value that has been prepaid or pre-funded, or in relation to transactions initiated using those Devices; and
- (b) without the service it would not be possible for a Direct Issuer Participant to be an Issuer or for another entity to be an Issuer through Sponsorship by a Direct Issuer Participant of the Scheme; and
- (c) the service (however named or described) relates to one or more of the following (each a Core Function) and only to one or more Core Functions:
 - (i) the licensing of the Scheme's brands and other intellectual property owned by, or licensed to, the administrator of the Scheme in Australia or any of its

Associated Entities, a licence (or sub-licence) of which is required in order to be a participant in the Scheme;

- (ii) connection to, and/or maintenance of a connection to, the systems to which it is necessary to connect in order to be a participant in the Scheme;
- (iii) transaction processing (including processing of charge-back transactions);
- (iv) clearing and settlement (including clearing and settlement of charge-back transactions);
- (v) authentication;
- (vi) authorisation;
- (vii) stand-in processing, clearing and settlement;
- (viii) fraud prevention; and
- (ix) handling, investigating and settling disputes, and requests or claims for chargebacks, raised by holders of Devices.

A service will relate only to one or more Core Functions for the purpose of this paragraph (c) even if it involves or includes incidental services necessary to support one or more Core Functions;

Credit Card Scheme means each payment system referred to as a 'Scheme' under *Standard No. 1 of 2016 The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers*;

Debit Card of a Scheme or Debit Card of that Scheme means, in relation to a Scheme, a Device issued by a participant in the Scheme in Australia under the Rules of the Scheme that can be used to make payments for goods or services by accessing a deposit account held at an authorised deposit-taking institution or a bank or other financial institution;

Debit Card Scheme means *Visa Debit, Debit MasterCard or the EFTPOS System*;

Debit Card Transaction means, in relation to a Scheme, a transaction in that Scheme between a holder of a Debit Card of that Scheme and a Merchant involving the purchase of goods or services (whether or not it also involves the obtaining of cash) using a Debit Card of that Scheme that is Acquired by an Acquirer (but does not include any transaction to reverse such a transaction or provide a credit or make a chargeback in relation to such a transaction);

Device means any card, plate or other payment code or device, including a code or device where no physical card or other embodiment is issued and a code or device used or to be used for only one transaction;

Direct Issuer Participant means, in relation to a Scheme, a participant in that Scheme in Australia as an Issuer, or as a Sponsor for one or more Issuers, that is not an Indirect Issuer Participant in that Scheme in Australia. Without limitation, for:

- (a) Debit MasterCard and MasterCard Prepaid this means any Principal Customer or Association Customer, each as defined in the Rules of the Scheme, in its capacity as Issuer or as Sponsor for one or more Issuers;
- (b) VISA Debit and Visa Prepaid this means any Principal-Type Member as defined in the Rules of the Scheme in its capacity as Issuer or as Sponsor for one or more Issuers; or
- (c) EFTPOS System and EFTPOS Prepaid this means:

- (i) any eftpos Issuer that is not an Indirect Settler; or
- (ii) any Settlement Agent,

with each of those expressions having the meaning given in the Rules of the Scheme;

Direct Issuer Participant Payments has the meaning given to it in clause 5.2;

Direct Issuer Participant Receipts has the meaning given to it in clause 5.2;

Dual-Network Debit Card or DNDC means a Debit Card of a Scheme (the 'First Scheme') that incorporates the functionality necessary to enable a transaction between the holder of the Device and a Merchant to be processed through:

(a) the payment network of the First Scheme; or

(b) the payment network of one or more of:

(i) the other Debit Card Schemes; and

(ii) any other payment system under which the holder of a Device may initiate or effect a transaction to make payments for goods or services by accessing a deposit account held at an authorised deposit-taking institution or a bank or other financial institution (whether or not the transaction also involves the obtaining of cash) provided that other payment system is not administered by the administrator of the First Scheme or any Associated Entity of the administrator of the First Scheme;

EFTPOS Scheme Rules are the rules promulgated under the constitution of EFTPOS Payments Australia Limited (ABN 37 136 180 366) and any schedule, document, specification or rule published by EFTPOS Payments Australia Limited pursuant to those rules;

Fair Value means, in relation to any Property or service:

(a) subject to paragraph (b), the amount that would be paid to acquire the Property or service in an orderly transaction between independent, unrelated and well informed parties at the earlier of:

- (i) the date the Property or service was first provided; and
- (ii) the date the Property or service was committed to be provided,

to the Direct Issuer Participant; but

(b) if at any subsequent time the amount that would be paid to acquire the Property or service in an orderly transaction between independent, unrelated and well informed parties (**Revised Value**) is materially different from the amount determined in accordance with paragraph (a) (or, if any adjustment is made in accordance with this paragraph (b), the most recent such adjustment), the Fair Value may be adjusted to that Revised Value provided:

- (i) use of that Revised Value as Fair Value is fair and reasonable and consistent with the objective of this Standard; and
- (ii) the Fair Value may be adjusted to a Revised Value no more than once in a Reporting Period;

Incentive Test: a Benefit meets the **Incentive Test** in relation to a Scheme Pair if it is given for a purpose of, or has or will likely have the effect of, any one or more of the following:

- (a) incentivising the entry into of a contract relating to the issue of Cards of any Scheme in the Scheme Pair;
- (b) promoting or incentivising the issuance or use of Cards of any Scheme in the Scheme Pair; or
- (c) providing or funding incentives to holders of Cards of any Scheme in the Scheme Pair to use those cards.

Benefits that meet the Incentive Test in relation to a Scheme Pair include lump-sum, volume based and transaction-specific Benefits such as:

- (i) incentives to market Cards of any Scheme in the Scheme Pair; and
- (ii) any of the following earned, accrued or receivable by a Direct Issuer Participant for agreeing to issue Cards of any Scheme in the Scheme Pair or for Card Transactions undertaken in any Scheme in the Scheme Pair meeting or exceeding a specific transaction volume, percentage share or dollar amount of transactions processed:
 - (A) a rebate on any fees or other costs or charges, whether for a Core Service or for any other product or service;
 - (B) a discount from the Regular Price of any Property or service, whether the Property or service is related to Cards of any Scheme in the Scheme Pair or not;

Indirect Issuer Participant means, in relation to a Scheme, a participant in that Scheme in Australia as an Issuer that participates in the Scheme in Australia as Issuer through the Sponsorship of another participant in that Scheme. Without limitation, for:

- (a) Debit MasterCard and MasterCard Prepaid this means any Affiliate Customer as defined in the Rules of the Scheme in its capacity as Issuer; or
- (b) VISA Debit and Visa Prepaid this means any Participant-Type Member or Associate-Type Member, each as defined in the Rules of the Scheme, in its capacity as Issuer; or
- (c) EFTPOS System and EFTPOS Prepaid this means any eftpos Issuer that is an Indirect Settler, with each of those expressions having the meaning given in the Rules of the Scheme;

Initial Reporting Period means, in relation to a New Issuer, the period commencing on the first date on which any Direct Issuer Participant Payments or Direct Issuer Participant Receipts were paid, became payable, were earned or accrued, or became receivable by or to the New Issuer (as applicable) and ending on the last day of the first full financial year following Public Launch by that New Issuer;

Interchange Fee Category has the meaning given to it in clause 4.1(b);

Interchange Fees means in relation to a Scheme, wholesale fees, known as interchange fees, which are payable between an Issuer and an Acquirer, directly or indirectly, in relation to Card Transactions in the Scheme but excluding any such fees to the extent that they are referable only to the obtaining of cash by the Card holder;

International Card Transaction means, in relation to a Scheme, a transaction in that Scheme that:

- (a) is between a holder of a Device issued by an International Issuer and a merchant in Australia;
- (b) involves the purchase of goods or services (whether or not it also involves the obtaining of cash); and

(c) is Acquired by an Acquirer,

but does not include any transaction to reverse such a transaction or provide a credit or make a chargeback in relation to such a transaction;

International Interchange Fee means, in relation to a Scheme, wholesale fees, known as interchange fees, which are payable between an International Issuer and an Acquirer, directly or indirectly, in relation to International Card Transactions in the Scheme but excluding any such fees to the extent that they are referable only to the obtaining of cash by the Device holder;

International Interchange Fee Category means a category of International Card Transactions in relation to which a particular International Interchange Fee applies, which may be:

(a) determined by reference to the nature of the holder or type of the Device, the identity or nature of the merchant, the means of effecting the transaction, the security or authentication that applies or any other matters; or

(b) a residual category covering transactions not in any other category;

International Issuer means a participant in a Scheme that has a contractual relationship with its customers under which it issues Devices of the Scheme to those customers or their nominees but that is not an Issuer;

International Multilateral Interchange Fee means, in relation to a Scheme, an International Interchange Fee that is determined by an administrator of the Scheme or any of its Associated Entities and applies regardless of the identity of the Acquirer or International Issuer paying or receiving the International Interchange Fee;

Issuer means a participant in a Scheme in Australia that has a contractual relationship with its customers under which it issues Debit Cards or Prepaid Cards of a Scheme (as the case may be) to those customers or their nominees;

Merchant means, in relation to a Scheme, a merchant in Australia that accepts a Card of that Scheme for payment for goods or services;

Multilateral Interchange Fee means, in relation to a Scheme, an Interchange Fee that is determined by an administrator of the Scheme and applies regardless of the identity of the Acquirer or Issuer paying or receiving the Interchange Fee;

Net Compensation has the meaning given to it in clause 5.1;

New Issuer means a Direct Issuer Participant in a Scheme that has not, before commencing the issue of any Cards of that Scheme, issued in Australia any Devices of any other Scheme or any Credit Card Scheme;

Public Launch in relation to a New Issuer, occurs when the New Issuer begins offering to issue Cards of a Scheme to its intended customer base and will not be taken to have occurred when a New Issuer has only issued Cards of that Scheme to its staff or a select group of its customers or other persons as part of a trial or test phase;

Prepaid Card of a Scheme or **Prepaid Card of that Scheme** means, in relation to a Scheme, a Device issued by a participant in the Scheme in Australia under the Rules of the Scheme that can be used to make payments for goods or services using a store of value that has been prepaid or pre-funded and is accessible to make payments for goods or services only through the use of that, or a linked or related, Device;

Prepaid Card Transaction means, in relation to a Scheme, a transaction in that Scheme between a holder of a Prepaid Card of that Scheme and a Merchant involving the purchase of goods or services (whether or not it also involves the obtaining of cash) using a Prepaid Card of that Scheme that is Acquired by an Acquirer (but does not include any transaction to reverse such a transaction or provide a credit or make a chargeback in relation to such a transaction);

Property means any property including any good and any proprietary right or interest;

Quarter means a 3 month period ending on 30 June, 30 September, 31 December or 31 March;

Reference Period means a 12 month period ending on the last day of a Quarter;

Regular Price means, in relation to Property or a service, a supplier and a Direct Issuer Participant at any time, the price at which the supplier is regularly supplying Property or services of the same description to entities of a class, group or type that includes the Direct Issuer Participant at that time;

Related Body Corporate has the meaning given in the *Corporations Act 2001*;

Relevant Portion has the meaning given to it in clause 5.2;

Reporting Period means a 12 month period ending 30 June;

Rules of a Scheme or **Rules of the Scheme** means the constitution, rules, by-laws, procedures and instruments of the relevant Scheme as applied in Australia, and any other arrangement relating to the Scheme by which participants in that Scheme in Australia are, or consider themselves to be, bound;

Scheme Benchmark is 8.0 cents;

Scheme Pair means:

- (a) VISA Debit and VISA Prepaid;
- (b) Debit MasterCard and MasterCard Prepaid; or
- (c) EFTPOS System and EFTPOS Prepaid;

Scheme Pair Transaction has the meaning given in clause 5.1;

Sponsor means:

- (a) in relation to a Scheme which is VISA Debit, VISA Prepaid, Debit MasterCard or MasterCard Prepaid, a participant in the Scheme in Australia who has accepted responsibility in whole or in part for, or to act as agent for, another entity under and in accordance with the Rules of the Scheme so that the other entity may participate in the Scheme; and
- (b) in relation to a Scheme which is EFTPOS System or EFTPOS Prepaid, a participant in the Scheme in Australia who has accepted responsibility to carry out settlement (the process of exchanging value to discharge payment obligations between Issuers and Acquirers), directly or indirectly, on behalf of one or more other entities,

and **Sponsorship** has a corresponding meaning;

SNDC Transaction means a Debit Card Transaction that is not effected using a DNDC;

include or **including** or **such as** when introducing an example do not limit the meaning of the words to which the example relates to that example or examples of a similar kind; and

terms defined in the Act have the same meaning in this Standard.

- 2.4 For the purposes of this Standard:
- (a) a provision of a plan, arrangement or agreement shall be deemed to have a particular purpose if the provision was included in the plan, arrangement or agreement by a party or parties for purposes that include that purpose and that purpose was a substantial purpose; and
 - (b) conduct including the payment or receipt of a fee or the giving of a benefit or other valuable consideration shall be deemed to have been made for a particular purpose if the person undertaking the conduct, payment or receipt did so for purposes that include that purpose and that purpose was a substantial purpose.
- 2.5 Each participant in a Scheme must do all things necessary on its part to ensure compliance with this Standard.
- 2.6 If any part of this Standard is invalid, this Standard is ineffective only to the extent of such part without invalidating the remaining parts of this Standard.
- 2.7 This Standard is to be interpreted:
- (a) in accordance with its objective; and
 - (b) by looking beyond form to substance.
- 2.8 For the purposes of this Standard, an Interchange Fee paid from an Acquirer to an Issuer is to be expressed as a positive number and an Interchange Fee paid from an Issuer to an Acquirer is to be expressed as a negative number.
- 2.9 On the Commencement Date this Standard replaces each of the following Standards:
- (a) *The Setting of Interchange Fees in the Visa Debit Payment System*; and
 - (b) *Interchange Fees in the EFTPOS System*.

Neither the registration nor the terms of this Standard affect those standards before the Commencement Date.

3. Anti-Avoidance

A participant in a Scheme must not, either alone or together with one or more other persons, enter into, begin to carry out or carry out a plan or arrangement or otherwise be knowingly involved in a plan or arrangement if it would be concluded that the person did so for a purpose of avoiding the application of this Standard, and the plan or arrangement or part of the plan or arrangement has achieved or would but for this provision have achieved or could reasonably be considered to have achieved that purpose.

4. Interchange Fees

- 4.1 (a) An Interchange Fee (exclusive of goods and services tax) in relation to a Card Transaction must:
- (i) where the Interchange Fee is a fixed amount per transaction and the Card Transaction is not a SNDC Transaction, not exceed ~~15~~10.0 cents; ~~or~~
 - (ii) where the Interchange Fee is a fixed amount per transaction and the Card Transaction is a SNDC Transaction, not exceed 6.0 cents; or

(iii) where the Interchange Fee is calculated by reference to the value or amount of the transaction, not exceed 0.200 per cent of that amount or value.

(b) If an Interchange Fee applies in relation to a category of Card Transactions (whether that category is determined by reference to the nature of the holder, or type of the Card of the Scheme, the identity or nature of the Merchant, the means of effecting the transaction, the security or authentication that applies or any other matter, or is a residual category covering transactions not in any other category) (**Interchange Fee Category**), that Interchange Fee must be:

- (i) a percentage of the value of the Card Transaction to which it relates; or
- (ii) a fixed amount,

applying to all Card Transactions in the category, and cannot be expressed as a range of rates or amounts.

4.2 If:

(a) the total value of Interchange Fees (exclusive of goods and services tax) payable in relation to Card Transactions undertaken in a Scheme during a Reference Period divided by the number of those Card Transactions exceeds the Scheme Benchmark; and

(b) for the Scheme Pair of which the Scheme referred to in sub-paragraph (a) forms part, the total value of Interchange Fees (exclusive of goods and services tax) payable in relation to Card Transactions undertaken in each of the Schemes in the Scheme Pair during the Reference Period divided by the number of those Card Transactions exceeds the Scheme Benchmark;

that Reference Period will be an **Above Benchmark Reference Period** for that Scheme and the participants in the Scheme referred to in paragraph (a) above must take all necessary steps to vary the rates or amounts of Interchange Fees applicable under that Scheme, with effect no later than 2 months and 1 day after the end of the Above Benchmark Reference Period, to rates or amounts such that, had those varied rates or amounts applied under the Scheme during the Above Benchmark Reference Period, that Reference Period would not have been an Above Benchmark Reference Period for that Scheme unless:

(c) prior to the end of that period of 2 months and 1 day, a variation to the rates or amounts of Interchange Fees applicable under the other Scheme in the Scheme Pair takes effect; and

(d) the varied Interchange Fees referred to in paragraph (c) are such that, had they applied under that other Scheme during the Above Benchmark Reference Period, the Reference Period would not have been an Above Benchmark Reference Period.

4.3 If at any time any Interchange Fee applicable under a Scheme is introduced or removed, or the rate or amount of any Interchange Fee under a Scheme is varied, the Interchange Fees applicable under that Scheme following that change must be such that, had they applied for the whole of the most recent Reference Period prior to the date of the change, that Reference Period would not have been an Above Benchmark Reference Period. Nothing in this clause 4.3 limits clause 4.2.

5. Net Payments to Direct Issuer Participants

- 5.1 ~~No~~Subject to clause 6.5, no Direct Issuer Participant in a Scheme may receive, directly or indirectly, Net Compensation in relation to Card Transactions undertaken in any of the Schemes in the Scheme Pair of which that Scheme forms part (**Scheme Pair Transactions**). **Net Compensation** is received by a Direct Issuer Participant if the Direct Issuer Participant Receipts of the Direct Issuer Participant for that Scheme Pair in respect of a Reporting Period exceed the Direct Issuer Participant Payments of the Direct Issuer Participant for that Scheme Pair in respect of that Reporting Period.
- 5.2 For the purpose of this clause 5:
- (a) subject to paragraphs (c), (d), (e), (f) and (g), **Direct Issuer Participant Receipts** of the Direct Issuer Participant for a Scheme Pair and a Reporting Period is the total of the Benefits that meet the Incentive Test in relation to that Scheme Pair that are earned or accrued during, or receivable in respect of, the Reporting Period by the Direct Issuer Participant and payable, allowable or otherwise to be provided, directly or indirectly, by the administrator in Australia of any Scheme in the Scheme Pair or any of the Associated Entities of any administrator in Australia of any Scheme in the Scheme Pair but, if such an Associated Entity is an Acquirer, excluding Interchange Fees;
 - (b) subject to paragraphs (c), (d), (e), (f) and (g), **Direct Issuer Participant Payments** of the Direct Issuer Participant for a Scheme Pair and a Reporting Period is the total amount paid or payable, directly or indirectly, by the Direct Issuer Participant to or in favour of the administrator in Australia of any Scheme in the Scheme Pair or any of the Associated Entities of any administrator in Australia of any Scheme in the Scheme Pair in relation to Core Services provided during or in respect of the Reporting Period for any of the Cards of the Schemes in the Scheme Pair or Scheme Pair Transactions.
 - (c) if a Benefit referred to in paragraph (a) or (b) does not relate solely to Cards of any Scheme in the Scheme Pair or Scheme Pair Transactions and also relates to other Devices or other transactions:
 - (i) the Benefit must be apportioned between:
 - (A) the Cards of any Scheme in the Scheme Pair and Scheme Pair Transactions on the one hand; and
 - (B) the other Devices and other transactions on the other,fairly and reasonably, having regard to, where relevant, the transaction history on Devices used in the payment systems to which the Benefit relates and the proportion of the Devices to which the Benefit relates that are Cards of a Scheme in the Scheme Pair issued by the Direct Issuer Participant or by any Indirect Issuer Participant through Sponsorship by that Direct Issuer Participant; and
 - (ii) the portion referable to Cards of any Scheme in the Scheme Pair and Scheme Pair Transactions determined in accordance with sub-paragraph (i) (the **Relevant Portion**) must be included in the determination of Direct Issuer Participant Receipts or Direct Issuer Participant Payments, as applicable;
 - (d) one method of apportionment under clause 5.2(c) that will be fair and reasonable for the purpose of that provision is an apportionment on a pro-rata basis, based on the value of Scheme Pair Transactions using Cards of any Scheme in the relevant Scheme Pair during the Reporting Period as a proportion of the total value of the transactions undertaken in any payment system to which the Benefit relates during the Reporting

Period. This does not preclude an apportionment in another way that meets the requirements of clause 5.2(c);

(e) where a Benefit referred to in paragraph (a), (b) or (c) relates to a period that spans more than one Reporting Period, the Benefit or, in the case of a Benefit referred to in paragraph (c), the Relevant Portion of the Benefit, may be allocated among Reporting Periods, in which case the allocation must:

- (i) be on a pro-rata basis based on the number of months in each relevant Reporting Period to which the Benefit relates if an allocation on that basis would fairly and reasonably align the Benefit to the activity to which the Benefit relates; or
- (ii) otherwise on some other basis that fairly and reasonably aligns the allocation of the Benefit to the activity to which the Benefit relates,

in each case provided that:

- (iii) no part of it is allocated to any Reporting Period the whole of which occurs before the term of the contract or arrangement under which the Benefit is payable, receivable or allowable has commenced;
- (iv) no part of it is allocated to any Reporting Period the whole of which occurs after the term of the contract or arrangement under which the Benefit is payable, receivable or allowable has ended; and
- (v) it may not be allocated among more than 10 consecutive Reporting Periods;

(f) a Direct Issuer Participant who adopts a particular method permitted by clause 5.2 of this Standard of:

- (i) determining whether and to what extent:
 - (A) Benefits are earned or accrued during, or are receivable in respect of, a Reporting Period for the purposes of paragraph 5.2(a); or
 - (B) Core Services are provided during or in respect of a Reporting Period for the purposes of paragraph 5.2(b); or

(ii) allocating or apportioning Benefits for the purpose of paragraph (c), (d) or (e),

must, unless the Reserve Bank of Australia otherwise agrees in writing, continue to use the same method consistently from one Reporting Period to the next; and

(g) for the purpose of this clause 5, a Direct Issuer Participant must ensure that:

- (i) a Benefit paid, allowed or otherwise provided, directly or indirectly, by the administrator of a Scheme in Australia or any of its Associated Entities that meets the Incentive Test in relation to the Scheme Pair of which that Scheme is part is included as a Direct Issuer Participant Receipt in the calculation of Net Compensation in respect of a Reporting Period; and
- (ii) an amount treated as a Direct Issuer Participant Payment in the calculation of Net Compensation in respect of a Reporting Period is not included as a Direct Issuer Participant Payment in the calculation of Net Compensation for any other Reporting Period.

6. Reporting and Transparency

6.1 An administrator of a Scheme in Australia or a representative of the participants in the Scheme in Australia must publish [on the Scheme's website](#):

(a) the Multilateral Interchange Fee rates or amounts (whichever is applicable) of the Scheme in Australia on the Scheme's website, including the rates or amounts for each Interchange Fee Category; and

(b) the International Multilateral Interchange Fee rates or amounts (whichever is applicable) of the Scheme, including the rates or amounts for each International Interchange Fee Category.

6.2 Each:

(a) Acquirer; and

(b) Issuer that is a Direct Issuer Participant,

that is a party to an agreement with one or more other participants in a Scheme to pay or receive Interchange Fees in relation to Card Transactions in the Scheme that are not Multilateral Interchange Fees must report to the Reserve Bank of Australia by 31 July each year the range of Interchange Fee rates or amounts (whichever is applicable) it received or paid in respect of the most recent Reporting Period. The Reserve Bank of Australia may publish the reported range of these Interchange Fees for the Scheme on its website.

6.3 An administrator of a Scheme in Australia or a representative of the participants in the Scheme in Australia must on or before 31 July each year certify in writing to the Reserve Bank of Australia in respect of the most recent Reporting Period, that Interchange Fees of the Scheme in Australia were during that Reporting Period in compliance with this Standard.

6.4 Each Subject to clause 6.5, each of an administrator of a Scheme in Australia and each Direct Issuer Participant in the Scheme in Australia must on or before 31 July each year certify in writing to the Reserve Bank of Australia that it was, in respect of the most recent Reporting Period, in compliance with clause 5.

6.5.5 Where a Direct Issuer Participant in a Scheme is a New Issuer, each of the administrator of the Scheme in Australia and the New Issuer will be taken to have complied with its obligations under clause 5 and clause 6.4 in respect of the period prior to and including the Initial Reporting Period if it:

(a) complies with clause 5 as if each reference to 'Reporting Period' is read as a reference to the Initial Reporting Period; and

(b) certifies in writing to the Reserve Bank of Australia that it was, in respect of the Initial Reporting Period, in compliance with clause 5 read as specified in clause 6.5(a) and provides such certification on or before 31 July in the year that the Initial Reporting Period ends.

6.6 An administrator of a Scheme in Australia or a representative of the participants of the Scheme in Australia must, not later than 30 days after the end of each Quarter, certify in writing to the Reserve Bank of Australia each of the following for that Quarter for the Scheme (and in the case of paragraph (e), the relevant Scheme Pair):

(a) the total value of Card Transactions undertaken in the Scheme in that Quarter;

(b) the number of Card Transactions undertaken in the Scheme in that Quarter;

(c) the total value of all Interchange Fees (exclusive of goods and services tax) payable in respect of the Card Transactions undertaken in the Scheme during that Quarter;

- (d) the total value of Interchange Fees (exclusive of goods and services tax) payable in respect of Card Transactions undertaken in the Scheme during the Quarter divided by the total number of the Card Transactions undertaken in the Scheme during the Quarter;
- (e) the total value of Interchange Fees (exclusive of goods and services tax) payable in respect of Scheme Pair Transactions undertaken in the Schemes that form part of that Scheme Pair during the Quarter divided by the total number of the Scheme Pair Transactions undertaken in the Schemes that form part of that Scheme Pair during the Quarter; and
- (f) each Interchange Fee Category that applied for some or all of the Quarter and, for each of those categories:
 - (i) the Interchange Fee rates or amounts (whichever is applicable) that applied during the Quarter (expressed as a percentage or an amount, not as a range); and
 - (ii) the total value of Interchange Fees (exclusive of goods and services tax) payable in respect of that Quarter that are referable to Card Transactions undertaken in the Scheme in that Quarter in that category.

7. Commencement and Implementation

- 7.1 This Standard came into force on the Commencement Date, but certain provisions in it had a transitional application as set out in clause 7 of this Standard as at the Commencement Date.
- 7.2 This Standard as varied with effect from 1 July 2019 must be complied with for the Reporting Period ending on 30 June 2020 and all subsequent Reporting Periods. For the Reporting Period ending on 30 June 2019 a Direct Issuer Participant in a Scheme in a Scheme Pair may elect to comply, in relation to both Schemes in that Scheme Pair, with either:
 - (a) this Standard as in effect on 30 June 2019; or
 - (b) this Standard as amended with effect on 1 July 2019 as if this Standard so amended had been in effect from 1 July 2018,
 and must notify its election of (a) or (b) (**Transitional Election**) to the administrator of each Scheme in the Scheme Pair no later than 1 July 2019.
- 7.3 An administrator of a Scheme in Australia that receives a notification under clause 7.2 from a Direct Issuer Participant must provide its certification of its compliance under clause 6.4 as that compliance relates to that Direct Issuer Participant and the Reporting Period ending on 30 June 2019 on the same basis as that specified in the Transitional Election made by that Direct Issuer Participant.
- 7.4 If a Direct Issuer Participant in a Scheme in a Scheme Pair does not give a Transitional Election in accordance with clause 7.2 then:
 - (a) it is taken to have elected to comply, in relation to both Schemes in that Scheme Pair, with this Standard as in effect on 30 June 2019; and
 - (b) the administrator of each Scheme in the Scheme Pair in Australia must provide its certification under clause 6.4 in relation to that Direct Issuer Participant and the Reporting Period ending on 30 June 2019 accordingly.

DRAFT STANDARD NO. 3 OF 2016

SCHEME RULES RELATING TO MERCHANT PRICING FOR CREDIT, DEBIT AND PREPAID CARD TRANSACTIONS

1. Objective

The objective of this Standard is to promote:

- *efficiency; and*
- *competition*

in the Australian payments system by providing for scheme rules that require participants to give merchants the freedom to make a charge for accepting payment of a particular kind that reflects the cost to the merchant of accepting that payment type.

2. Application

2.1. This Standard is determined under Section 18 of the Payment Systems (Regulation) Act 1998 (the **Act**).

2.2. This Standard applies to each of the following, each of which is referred to in this Standard as a **Scheme**:

(a) the payment system operated within Australia known as the MasterCard system, which was designated under the Act as a payment system on 12 April 2001 and which is referred to in this Standard as the **MasterCard System**;

(b) the payment system operated within Australia known as the VISA system, which was designated under the Act as a payment system on 12 April 2001 and which is referred to in this Standard as the **VISA System**;

~~(c) the American Express Companion Card payment system operated within Australia, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as the **American Express Companion Card Scheme**;~~

~~(d)~~(c) the payment system operated within Australia known as Visa Debit, which was designated under the Act as a payment system on 23 February 2004 and which is referred to in this Standard as **Visa Debit**;

~~(e)~~(d) the payment system operated within Australia known as Debit MasterCard, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as **Debit MasterCard**;

~~(f)~~(e) the debit card payment system operated within Australia known as the EFTPOS payment system, which was designated under the Act as a payment system on 12 June 2012 and which is referred to in this Standard as the **EFTPOS System**;

~~(g)~~(f) the prepaid card payment system operated within Australia under the EFTPOS Scheme Rules, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as **EFTPOS Prepaid**;

~~(h)~~(g) the payment system operated within Australia known as MasterCard Prepaid, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as **MasterCard Prepaid**; and

(+)(h) the payment system operated within Australia known as Visa Prepaid, which was designated under the Act as a payment system on 15 October 2015 and which is referred to in this Standard as **Visa Prepaid**.

2.3. In this Standard:

Acquired or **Acquiring** includes accepted or accepting;

Acquirer means a participant in a Scheme in Australia that:

- a) provides services, directly or indirectly, to a Merchant to allow the Merchant to accept a Card of that Scheme; or
- b) is a Merchant that accepts, or is a Related Body Corporate of a Merchant that accepts, a Card of that Scheme and bears risk as principal in relation to the payment obligations of the Issuer of that Card in relation to that acceptance;

Acquirer Supplied Element means in relation to an Acquirer, a Merchant and a Scheme, those of the Permitted Cost of Acceptance Elements for that Merchant and that Scheme that are supplied, directly or indirectly, by that Acquirer;

Card, Card of a Scheme or **Card of that Scheme** means a Credit Card of a Scheme, Debit Card of a Scheme or Prepaid Card of a Scheme;

Card Transaction means a Credit Card Transaction, Debit Card Transaction or Prepaid Card Transaction;

Commencement Date means 1 September 2016;

Cost of Acceptance has the meaning given to it in clause 0;

Credit Card, Credit Card of a Scheme or **Credit Card of that Scheme** means, in relation to a Scheme, a Device that can, under the Rules of the Scheme, be used in Australia for purchasing goods or services on credit (irrespective of whether the Device is issued in or outside Australia);

Credit Card Scheme means ~~the American Express Companion Card Scheme,~~ the MasterCard System or the VISA System;

Credit Card Transaction means, in relation to a Credit Card Scheme, a transaction in that Scheme between a holder of a Credit Card of that Scheme and a Merchant involving the purchase of goods or services using a Credit Card of that Scheme that is Acquired by an Acquirer and includes any transaction to reverse such a transaction or provide a credit or make a chargeback in relation to such a transaction;

Debit Card, Debit Card of a Scheme or **Debit Card of that Scheme** means, in relation to a Scheme, a Device that can, under the Rules of the Scheme, be used in Australia to make payments to Merchants for goods or services by accessing a deposit account held at an authorised deposit-taking institution or a bank or other financial institution (irrespective of whether the Device is issued in or outside Australia);

Debit Card Scheme means Debit MasterCard, the EFTPOS System or Visa Debit;

Debit Card Transaction means, in relation to a Debit Card Scheme, a transaction in that Scheme between a holder of a Debit Card of that Scheme and a Merchant involving the purchase of goods or services (whether or not it also involves the obtaining of cash) using a Debit Card of that Scheme that is Acquired by an Acquirer and includes any transaction to reverse such a transaction or provide a credit or make a chargeback in relation to such a transaction;

Device means any card, plate or other payment code or device, including a code or device where no physical card or other embodiment is issued and a code or device used or to be used for only one transaction;

EFTPOS Scheme Rules means the rules promulgated under the constitution of EFTPOS Payments Australia Limited (ABN 37 136 180 366) and any schedule, document, specification or rule published by EFTPOS Payments Australia Limited pursuant to those rules;

Financial Year means a period from 1 July to the following 30 June;

Issuer means an entity that issues Cards of a Scheme to its customers;

Large Merchant means a Merchant that satisfies two or all of the following:

- (a) the consolidated gross revenue for the Financial Year ended 30 June 2015 of the Merchant and its Related Bodies Corporate was \$25 million or more;
- (b) the value of the consolidated gross assets at 30 June 2015 of the Merchant and its Related Bodies Corporate was \$12.5 million or more;
- (c) as at 30 June 2015 the Merchant and its Related Bodies Corporate between them had 50 or more employees (whether full time, part time, casual or employed on any other basis);

Merchant means, in relation to a Scheme, a merchant in Australia that accepts a Card of that Scheme for payment for goods or services;

Merchant Service Fee means a transaction-based fee (or a time-period-based fee that covers a specified or maximum number of transactions) charged to a Merchant by an Acquirer for Acquiring, or by a Payment Facilitator for arranging the Acquisition of, one or more types of Card Transaction from that Merchant whether collected on an ad valorem or flat-fee basis, or charged as a blended or bundled rate across more than one type of Card Transaction or on an interchange plus acquirer margin basis or any other basis;

Payment Facilitator means an entity which arranges or procures Acquiring services from an Acquirer for one or more Merchants;

Payment Service Provider means, in relation to a Merchant and a Scheme, an entity that is not a Related Body Corporate of the Merchant that provides services and/or equipment to the Merchant that directly relate to, or are directly used for or in connection with, the acceptance by that Merchant of Cards of that Scheme for payment for goods or services;

Permitted Cost of Acceptance Elements in relation to a Merchant and a Scheme are the fees and premiums referred to in clause 1.1.11(a) for that Merchant and that Scheme;

Permitted Surcharge has the meaning given to it in clause 4.1;

Prepaid Card, Prepaid Card of a Scheme or Prepaid Card of that Scheme means, in relation to a Scheme, a Device that can be used in Australia, under the Rules of the Scheme, to make payments for goods or services using a store of value that has been prepaid or pre-funded and is accessible to make payments for goods or services only through the use of that, or a linked or related, Device (irrespective of whether the Device is issued in or outside Australia);

Prepaid Card Scheme means EFTPOS Prepaid, MasterCard Prepaid or Visa Prepaid;

Prepaid Card Transaction means in relation to a Prepaid Card Scheme a transaction in that Scheme between a holder of a Prepaid Card and a Merchant involving the purchase of

goods or services (whether or not it also involves the obtaining of cash) using a Prepaid Card relating to that Scheme and includes any transaction to reverse such a transaction or provide a credit or make a chargeback in relation to such a transaction;

Reference Period has the meaning given to it in clause 0;

Related Body Corporate has the meaning given in the *Corporations Act 2001*;

Rules of a Scheme or **Rules of the Scheme** means the constitution, rules, by-laws, procedures and instruments of the relevant Scheme, and any other arrangement relating to the Scheme by which participants in that Scheme are, or consider themselves to be, bound;

Scheme Pair means:

- (a) Visa Debit and Visa Prepaid;
- (b) Debit MasterCard and MasterCard Prepaid; or
- (c) EFTPOS System and EFTPOS Prepaid;

Statement Period has the meaning given to it in clause 1.1.11(a);

Surcharge means, in respect of any Card Transaction, any of the following, however named or described:

- (a) an amount charged, in addition to the price of goods or services, for the relevant Merchant accepting payment through the Card Transaction; or
- (b) an amount charged for making payment through the Card Transaction. An amount will be charged for making payment through a Card Transaction if:
 - (i) that amount is charged because the purchase of the relevant goods or services is effected using the relevant Card; or
 - (ii) the goods or services could be purchased from the relevant Merchant by a different payment method without that amount being charged;

include or **including** or **such as** when introducing an example do not limit the meaning of the words to which the example relates to that example or examples of a similar kind; and terms defined in the Act have the same meaning in this Standard.

- 2.4. Each participant in a Scheme must do all things necessary on its part to ensure compliance with this Standard.
- 2.5. If any part of this Standard is invalid, this Standard is ineffective only to the extent of such part without invalidating the remaining parts of this Standard.
- 2.6. This Standard is to be interpreted:
 - (a) in accordance with its objective; and
 - (b) by looking beyond form to substance.
- 2.7. This Standard shall not apply in respect of Rules of a Scheme that relate, or the conduct of participants in a Scheme that relates, to charges made by Merchants for accepting Cards for payment of a taxi fare in a State or Territory of Australia. Accordingly payment of a taxi fare in any State or Territory of Australia effected using a Card is not a payment of a kind covered by this Standard.

- 2.8. This Standard replaces each of the following Standards or parts of Standards:
- (a) each of Standard No. 2 *Merchant Pricing for Credit Card Purchases* which applied to the MasterCard System and Standard No. 2 *Merchant Pricing for Credit Card Purchases* which applied to the VISA System; and
 - (b) clauses 9 and 10 and sub-clauses 12 (i), (ii) and (iii) of The Honour All Cards Rule in the Visa Debit and Visa Credit Card Systems and the No Surcharge Rule in the Visa Debit System Standard.

3. Merchant Pricing

Neither the Rules of a Scheme nor any participant in a Scheme shall prohibit or deter:

- (a) a Merchant from recovering, by charging a Surcharge in respect of a Card Transaction in a Scheme at any time, an amount that does not exceed the Permitted Surcharge for that Merchant and that Scheme at that time; or
- (b) a Merchant, in recovering part or all of the Cost of Acceptance of Cards of the Scheme, from applying different Surcharges in respect of Card Transactions in different Schemes (except that, in relation to a Scheme Pair, the Rules of a Scheme may require that if a Surcharge is applied in respect of Card Transactions in one Scheme in the Scheme Pair, any Surcharge applied in respect of Card Transactions in the other Scheme in the Scheme Pair must be the same).

4. Permitted Surcharge

- 4.1. The Permitted Surcharge for a Merchant and a Scheme at any time is an amount not exceeding the Cost of Acceptance for that Merchant and that Scheme applicable at that time.
- 4.2. For the purpose of clause 0 the Cost of Acceptance of Cards of a Scheme applicable at a time is:
- (a) subject to paragraph (b), the Cost of Acceptance of Cards of the Scheme calculated for a 12 month period that ended not more than 13 months before that time; or
 - (b) if the Cost of Acceptance of Cards of the Scheme for a Merchant for a 12 month period preceding that time is not reasonably ascertainable, an estimate of the average cost of acceptance of Cards of the Scheme for a period of 12 months calculated by the Merchant in good faith using only known and/or estimated Permitted Cost of Acceptance Elements and Card Transaction volumes for Cards of the Scheme.

Each 12 month period referred to in paragraph (a) or paragraph (b) is a **Reference Period**.

5. Cost of Acceptance

- 5.1. Subject to the other provisions of this clause 0, Cost of Acceptance for a Merchant, a Scheme and a Reference Period at any time means, in relation to the Merchant's acceptance of a Card of the Scheme, the average cost per Card Transaction in the Scheme calculated for the Reference Period as follows:
- (a) by adding only the following amounts paid by the Merchant in respect of that Scheme during that Reference Period, which are to be determined taking into account any discount, rebate or other allowance received or receivable by the Merchant to the extent any such discount, rebate or other allowance is ascertainable:

- (i) the applicable Merchant Service Fee or Merchant Service Fees in respect of Card Transactions in the Scheme;
- (ii) fees paid to any entity that was the Merchant's Acquirer, Payment Facilitator or Payment Service Provider during the Reference Period for:
 - (A) the rental and maintenance of payment card terminals that process Cards of that Scheme; or
 - (B) providing gateway or fraud prevention services referable to that Scheme;
- (iii) fees incurred in processing Card Transactions in that Scheme and paid to any entity that was the Merchant's Acquirer or Payment Facilitator during the Reference Period including international service assessments or cross-border transaction fees, switching fees and fraud-related chargeback fees (but, for the avoidance of doubt, excluding the amount of chargebacks); and
- (iv) if the Merchant acts as agent for a principal, fees or premiums paid by the Merchant to an entity that is not a Related Body Corporate of the Merchant to insure against the risk that the Merchant will be liable to a customer for the failure of its principal to deliver goods or services purchased through a Card Transaction provided that such risk arises because payment for the relevant goods or services is effected through a Card Transaction,

but in each case only if those fees or premiums are:

- (v) directly related to Card Transactions in that Scheme. A fee or premium will not be so directly related if it is incurred in relation to or in connection with a payment, or the sale or purchase to which the payment relates, irrespective of the method used to make the payment; and
- (vi) subject to clause 1.1.11(b), documented or recorded in:
 - (A) a contract in effect between the Merchant and its Acquirer, Payment Facilitator or Payment Service Provider that relates to or covers the Scheme or Card Transactions in the Scheme (whether or not it also relates to or covers other Schemes or Card Transactions in other Schemes); or
 - (B) a statement or invoice from the Merchant's Acquirer, Payment Facilitator or Payment Service Provider that relates to or covers the Scheme or Card Transactions in the Scheme; and
- (b) expressing the total of the amounts in paragraph (a) above as a percentage of the total value of Card Transactions in the Scheme between the Merchant and holders of Cards in the Scheme in that Reference Period, with that percentage being the average cost per Card Transaction in the Scheme.

5.2. In relation to a Merchant's acceptance of a Card of a Scheme that is part of a Scheme Pair **Cost of Acceptance** for a Reference Period will be calculated as provided in clause 0, except that the average cost per Card Transaction for the Reference Period must be calculated across the Scheme Pair using only the Permitted Cost of Acceptance Elements for both Schemes in the Scheme Pair.

5.3 If a Permitted Cost of Acceptance Element is not levied or charged on a per transaction basis and is not referable only to Card Transactions undertaken in a single Scheme (or Scheme Pair where clause 0 applies) (for example, a fixed monthly terminal rental cost that allows Card Transactions in more than one Scheme to be made), that Permitted Cost of

Acceptance Element is to be apportioned among the relevant Schemes, Scheme Pairs and other payment systems (as the case may be) to which it relates for the purpose of determining Cost of Acceptance on a pro-rata basis. The apportionment is to be based on the value of the Card Transactions in the relevant Scheme or Scheme Pair (as applicable) over the period to which the cost relates as a proportion of the total value of transactions undertaken in any payment system to which the cost relates over that period (in each case, the value of the Card Transactions and transactions excludes the amount of any cash obtained by the holder of a Card of a Scheme or other Device as part of a Card Transaction or other transaction).

6. Card Identification

- 6.1. All Debit Cards issued after 1 July 2017 in Australia by a participant in a Debit Card Scheme that are capable of being visually identified as Debit Cards must be so identified. All Prepaid Cards issued after 1 July 2017 in Australia by a participant in a Prepaid Card Scheme that are capable of being visually identified as Prepaid Cards must be so identified.
- 6.2. All Debit Cards issued in Australia by a participant in a Debit Card Scheme must be issued with a Bank Identification Number (**BIN**) that allows them to be electronically identified as Debit Cards. All Prepaid Cards issued after 1 July 2017 in Australia by a participant in a Prepaid Card Scheme in Australia must be issued with a BIN that allows them to be electronically identified as Prepaid Cards.
- 6.3. Without limiting clause 0:
 - (a) an administrator of a Scheme in Australia or an Acquirer that Acquires both Credit Card Transactions and Debit Card Transactions for a Merchant must provide to the Merchant, or publish, lists of BINs that permit the Merchant to separately identify Credit Card Transactions and Debit Card Transactions electronically; and
 - (b) from 1 July 2017, an administrator of a Scheme in Australia or an Acquirer that Acquires Card Transactions of more than one Scheme for a Merchant must provide to the Merchant, or publish, lists of BINs that permit the Merchant to separately identify Card Transactions of each applicable Scheme electronically.

7. Transparency

- 7.1. Subject to clause 0, each Acquirer must, on or as soon as practicable after the Commencement Date, notify in writing each Merchant for which the Acquirer directly or indirectly provides Acquiring services of the provisions of this Standard.
- 7.2. Subject to clause 0, each Acquirer must issue, or cause to be issued, monthly statements to each Merchant for which the Acquirer provides Acquiring services, directly or indirectly. Each such statement must set out:
 - (a) the dates on which the period covered by the statement begins and ends (**Statement Period**). For that purpose, for all statements except the first, the date a statement period begins must be the day after the day the immediately previous statement period ends;
 - (b) for the relevant Statement Period:
 - (i) the aggregate cost of the Acquirer Supplied Elements of the Cost of Acceptance for the Merchant of:

- (A) Credit Cards of each applicable Credit Card Scheme; and
 - (B) Debit Cards and Prepaid Cards of each applicable Scheme Pair,
- over the Statement Period (each such aggregate being a **Month Element Cost Total**);
- (ii) the aggregate value of Card Transactions Acquired for the Merchant for:
 - (A) each applicable Credit Card Scheme; and
 - (B) each applicable Scheme Pair,
 over the Statement Period (each such aggregate being a **Month Value Total**);
and
 - (iii) for each applicable Credit Card Scheme and each applicable Scheme Pair, the Month Element Cost Total expressed as a percentage of the corresponding Month Value Total; and
- (c) if it is the statement for the last full Statement Period within a Financial Year:
- (i) the aggregate cost of the Acquirer Supplied Elements of the Cost of Acceptance for the Merchant over the 12 month period ending on the last day of that Statement Period (an **Annual Period**) of:
 - (A) Credit Cards of each applicable Credit Card Scheme; and
 - (B) Debit Cards and Prepaid Cards of each applicable Scheme Pair,
 (each such aggregate being an **Annual Element Cost Total**);
 - (ii) the aggregate value of Card Transactions Acquired for the Merchant for:
 - (A) each applicable Credit Card Scheme; and
 - (B) each applicable Scheme Pair,
 over the Annual Period (each such aggregate being an **Annual Value Total**); and
 - (iii) for each applicable Credit Card Scheme and each applicable Scheme Pair, the Annual Element Cost Total expressed as a percentage of the corresponding Annual Value Total.

7.3. An Acquirer will not contravene clause 0 or 0 if:

- (a) the Acquirer provided Acquiring services to the Merchant indirectly via a Payment Facilitator;
- (b) prior to the time the Acquirer was required to notify or give a statement under clause 0 or 0 (as applicable), it entered into a written agreement with the Payment Facilitator which obliged the Payment Facilitator to provide the notice and statements described in clauses 0 and 0 at the times described in those clauses;
- (c) after conducting due inquiries of the Payment Facilitator before that agreement was entered into, the Acquirer was satisfied that the Payment Facilitator had sufficient processes in place to provide those notices and statements at the times described in clauses 0 or 0 (as applicable); and
- (d) after entering into that agreement and prior to the time the notice or statement (as the case may be) was required to be sent, the Acquirer had not had cause to suspect

that the notice or statement would not be sent to the Merchant by the Payment Facilitator in accordance with clauses 0 or 0 (as applicable).

8. Anti-Avoidance

- 8.1. A participant in a Scheme must not, either alone or together with one or more other persons, enter into, begin to carry out or carry out a plan or arrangement or otherwise be knowingly involved in a plan or arrangement if it would be concluded that the person did so for a purpose of avoiding the application of this Standard, and the plan or arrangement or part of the plan or arrangement has achieved or would but for this provision have achieved or could reasonably be considered to have achieved that purpose.
- 8.2. For the purpose of this Standard, a provision of a plan or arrangement shall be deemed to have a particular purpose if the provision was included in the plan or arrangement by a party or parties for purposes that include that purpose and that purpose was a substantial purpose.
- 8.3. Without limiting clause 0, neither the Rules of a Scheme, nor a participant in a Scheme, shall directly or indirectly deny a Merchant access to Acquiring services or decline to provide Acquiring services to a Merchant for the reason (whether solely or in combination with other reasons) that:
 - (a) the Merchant imposes or intends to impose a Surcharge in relation to Card Transactions in that Scheme; or
 - (b) the amount of any Surcharge charged, or proposed to be charged, by the Merchant in relation to Card Transactions in the Scheme is a particular amount, either in absolute terms or relative to any other Surcharge (unless that amount would exceed the Permitted Surcharge for Card Transactions in that Scheme).

9. Commencement and implementation

- 9.1. This Standard comes into force on the Commencement Date, but certain provisions in it have a deferred commencement as set out in this clause 0.
- 9.2. Without limiting clause 0, the provisions of clauses 0, 0 and 0 will apply in relation to a Merchant that is a Large Merchant on and from the Commencement Date.
- 9.3. The provisions of clauses 0, 0 and 0 will not apply in relation to a Merchant that is not a Large Merchant until 1 September 2017, on which date clauses 0, 0 and 0 will commence to apply in relation to Merchants that are not Large Merchants.
- 9.4. For the period from the Commencement Date until 31 August 2017 the following will apply in relation to Merchants that are not Large Merchants:
 - (a) neither the Rules of a Scheme nor any participant in a Scheme shall prohibit:
 - (i) a Merchant from recovering, by charging a Surcharge in respect of a Card Transaction in a Scheme at any time, part or all of the reasonable cost of acceptance of Cards issued under the Scheme at that time; or
 - (i) a Merchant, in recovering part or all of the reasonable cost of acceptance of Cards of a Scheme, from applying different Surcharges in respect of Card Transactions in different Schemes; and

(b) for the purposes of paragraph (a), a Merchant's cost of acceptance of Cards issued under a Scheme may, for the purpose of determination of a Surcharge, be determined by reference to:

- (i) the cost to the Merchant of the Card Transaction in relation to which the Surcharge is to be levied;
- (ii) the average cost to the Merchant of acceptance of all Cards of all types issued under the Scheme; or
- (iii) the average cost to the Merchant of acceptance of a subset of Cards issued under the Scheme that includes the type of Card in relation to which the Surcharge is to be levied,

and includes, but is not necessarily limited to, in the case of (i), the applicable Merchant Service Fee and, in the case of (ii) and (iii), all applicable Merchant Service Fees.

9.5. The provisions of clauses 0 and 0 will not apply until 1 June 2017, on which date those clauses will commence to apply. For the avoidance of doubt, a monthly statement issued on or after 1 June 2017 relating to a Statement Period ending during June 2017 must contain:

- (a) the information required by clause 1.1.11(b) in relation to the Statement Period to which that statement relates even though that Statement Period may have commenced before 1 June 2017; and
- (b) the information required by clause 1.1.11(c) in relation to the Annual Period ending on the last day of the Statement Period to which that statement relates even though that Annual Period commenced before 1 June 2017.