

Review of Card Payments Regulation

Conclusions Paper

May 2016

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1. Executive Summary

This document represents the conclusions of the Reserve Bank of Australia's Review of Card Payments Regulation. The Review commenced in March 2015 with publication of an Issues Paper that highlighted developments in the cards market and aspects of the regulatory framework that warranted review.¹ After extensive public consultation, the Bank released a Consultation Paper in December that outlined the Payments System Board's preliminary views on the major issues and presented a draft set of standards for consultation.² The Bank again consulted extensively with a wide range of stakeholders and is now releasing a final set of standards which, in the opinion of the Board, will contribute to a more efficient and competitive payments system.

The Review was a comprehensive examination of the regulatory framework, guided by the Board's mandate to promote competition and efficiency in the payments system. In assessing the case for changes the Board was mindful of the interrelationships between different aspects of the existing regulatory framework and considered how possible changes might best fit together as a cohesive package. The key issues for the Review fell into three broad but interrelated categories.

The first was efficiency issues related to interchange fees and the transparency of card payments that are discussed in Chapter 3. The major considerations were: whether the current average interchange fee levels are inefficiently high; the implications of the widening of the range of interchange fees for the transparency of payment costs to merchants; if the coverage of the interchange benchmarks was appropriate; and whether compliance with the current benchmarks could be made more effective. Overall, the Board has reaffirmed its view that there is little justification for significant interchange fees in mature card systems and that there is an ongoing role for regulatory intervention in the cards market because of the perverse ways in which competition between card schemes can play out.

The key decisions regarding the Bank's interchange standards are:

- The weighted-average interchange fee benchmark for debit cards has been reduced to 8 cents per transaction, which will apply jointly to debit and prepaid cards in each scheme.
- The weighted-average benchmark of 0.50 per cent for credit cards will be maintained.
- The weighted-average benchmarks will be supplemented by ceilings on individual interchange rates: 0.80 per cent for credit; and 15 cents, or 0.20 per cent if the interchange fee is specified in percentage terms, for debit and prepaid.
- To prevent interchange fees drifting upwards in the manner that they have previously, compliance with the benchmark will be observed quarterly rather than every three years.
- Commercial cards will continue to be included in the benchmark and will be subject to the ceilings above.

1 See RBA (2015a).

2 See RBA (2015b).

- Transactions on foreign-issued cards acquired in Australia will for the present remain outside the benchmark, in light of commitments from schemes to ensure that the Bank's standards are not circumvented. The Board will take careful note of developments in this area.
- The new interchange benchmarks will take effect from 1 July 2017.

The second set of issues pertained to the implications of regulation applying to some payment systems but not to others. This had given rise to concerns that the regulatory framework was not fully competitively neutral, which was significantly influencing market developments. A particular focus was on the American Express companion card system. This raised the question of whether interchange-like payments from three-party schemes to issuers (notably in the American Express companion card system) should be regulated in the same way as interchange fees in standard four-party business models; this issue is addressed in Chapter 4.

The key decisions regarding competitive neutrality are:

- In October, the Board designated the American Express companion card system after concluding that it would be in the public interest to do so.
- Interchange-like payments to issuers in the American Express companion card system will be subject to equivalent regulation as applies to the MasterCard and Visa credit card systems.
- To prevent possible circumvention of the debit and credit card interchange standards there will now be limits on any scheme payments to issuers that are not captured with the interchange benchmarks.

The third set of issues related to surcharging practices; these are addressed in Chapter 5. The right of merchants to surcharge for expensive payment methods is important for payments system efficiency and helps to hold down the cost of goods and services to consumers generally. However, there have been concerns in recent years that merchants in some industries have been surcharging above the cost of acceptance for some transactions, particularly in the case of some fixed-dollar surcharges. The Government recently legislated to give the Australian Competition and Consumer Commission (ACCC) enforcement power over excessive surcharges. The Bank is now modifying its surcharging standards to respond to the issues raised in the Review, with the new standard also specifying a 'permitted surcharge' for the purposes of the new legislation.

The key decisions regarding surcharging are:

- The Bank's standard now defines the 'permitted surcharge' on a card transaction in terms of the merchant's average cost of acceptance for each scheme.
- The breadth of costs included in the permitted surcharge is somewhat narrower than under the Bank's current guidance note.
- The average cost of acceptance is defined in percentage terms implying that merchants will not be able to levy high fixed-amount surcharges on low-value transactions.
- Acquirers and payment facilitators will be required to provide merchants with easy-to-understand information on the cost of acceptance for each scheme from 1 June 2017.
- The new framework for surcharging will take effect for large merchants on 1 September 2016 and on 1 September 2017 for other merchants.

2. Introduction

This document represents the Board’s conclusions and includes final standards that have been registered on the Federal Register of Legislation concurrent with publication of this document. This chapter outlines the background and process for the Review, in the context of the Board’s mandate and competition and efficiency considerations. Chapters 3, 4 and 5 cover the key issues for the Review: efficiency issues related to interchange fees and the transparency of card payments; competitive neutrality of card payments regulation; and excessive surcharging. Each chapter describes the key issues, stakeholders’ views, the Boards’s assessment and any significant changes to the regulatory framework. Chapter 6 describes the final standards in more detail and highlights the main changes relative to the draft standards that were released for consultation in December 2015.

2.1 Background to the Review

Following the Wallis Inquiry in 1997, the Bank was assigned a number of responsibilities and powers in relation to the payments system and the Board was established to oversee this mandate.³ The Board is required to exercise its responsibilities in a way that promotes a safe, efficient and competitive payments system (section 2.3).

In the early 2000s, the Bank began implementing a series of reforms to card payments regulation. These reforms included measures that changed the relative prices cardholders faced when using debit and credit cards, reducing the incentives to use higher-cost payment methods. The Bank’s reforms also required changes to certain restrictive rules in card systems, including to allow merchants to apply surcharges on card transactions so that cardholders were more likely to face prices that reflected the cost of the card they were using. The Bank also took steps that reduced the barriers to entry for entities wishing to issue cards or provide card payment services to merchants.

In 2007–08, the Board conducted a review of the Bank’s reforms. The review concluded that the reforms had improved access, increased transparency and had led to more appropriate price signals to consumers. This review also explored a number of options for possible changes to the regulatory framework, including stepping back from formal regulation and relying on industry undertakings. However, the industry was unable to arrive at suitable undertakings, so in August 2009 the Board decided against stepping back from interchange regulation and noted that the regulatory framework would remain under review.

The first major review of the financial system since the Wallis Inquiry was announced by the Government in 2013. The Final Report of the Financial System Inquiry (FSI), released in December 2014, endorsed the reforms undertaken by the Board since it was established.⁴ It also recommended that the Bank further consider elements of card payments regulation, particularly in relation to interchange fees and surcharging. The Bank had also raised concerns about aspects of the interchange

³ See Financial System Inquiry (1997).

⁴ See Financial System Inquiry (2014).

fee system and merchant surcharging practices in its submission to the FSI, including a decline in transparency for some end users, perceptions of excessive surcharging in some industries, and questions around whether existing regulation was fully competitively neutral.

2.2 The Review process

The Bank's Review of Card Payments Regulation commenced in March 2015 with the publication of an Issues Paper that sought the views of stakeholders and interested parties on the regulatory framework, including on issues that the Bank had raised in its March 2014 submission to the FSI (RBA 2014) and on issues that the FSI had identified in its Interim and Final Reports (see Box A). The Bank received over 40 written submissions in response to the Paper and also considered submissions on card payments regulation to the FSI. Some submissions raised issues that had not been canvassed in the Issues Paper, particularly with regard to the coverage of interchange caps. Consultations were conducted both individually, and collectively, when the Bank hosted a roundtable discussion that brought together stakeholders from the payments industry, end users of payments services and government.

In August 2015, the Board asked Bank staff to liaise with industry participants on the possible designation of the bank-issued American Express companion card system, the Debit MasterCard system and the eftpos, MasterCard and Visa prepaid card systems. The Bank determined that it would be in the public interest to designate these systems and, following a resolution of the Board, did so in October. The designation of a system is the first of a number of steps that the Bank must take to exercise any of its powers, such as imposing an access regime or setting standards.

The Bank released draft standards for card payments regulation for public consultation on 3 December 2015. Over 40 organisations and individuals made written submissions; the majority of these were published on the Bank's website, while some were submitted in confidence. The Bank also received a significant number of emails on surcharging and on interchange as part of two coordinated campaigns on these issues. The Bank conducted around 50 consultation meetings with interested parties, including a range of stakeholders that had not provided written submissions, as well as those that did.

The release of the Bank's draft standards coincided with the Government introducing legislation to ban excessive surcharges on card payments, which was subsequently passed by Parliament on 22 February 2016 (see Box B). Under the new law, the ACCC will enforce a ban on excessive surcharging and will, in the case of card payments, rely on the Bank's surcharging standard to determine the level of surcharge that is permitted. The Bank has been working closely with Treasury and the ACCC to ensure that the surcharging regime is as clear as possible for the industry, merchants, consumers and regulators.

The conclusions presented in this document address most of the matters raised in the Bank's March 2015 Issues Paper. One matter not specifically addressed is issues arising with respect to competing payment options on a single device – this includes both issues that have arisen in the case of dual-network debit cards and those that may arise in the case of electronic wallets. Newer form factors, such as electronic wallets, potentially allow a consumer to access a wider range of different cards (or other means of payment) for a given transaction than in the past. This gives rise to a number of regulatory issues, including the possibility that technology, telecommunications or payment providers may seek to restrict the choice of options available to end users and financial institutions. Innovations in the payment process, such as tokenisation, might also be used in ways that restrict competition, for

example, where a network requires that a transaction be processed via a particular tokenisation service. The Review has not focused on policy responses in this area given that they are largely separate from the main public-interest issues addressed here and involve some complex issues arising from developments in technology. The Bank will, however, continue to monitor developments in this area and will consider the appropriate response where significant issues arise.

Box A: Financial System Inquiry (FSI) Recommendations

The FSI Final Report made two recommendations with respect to payments regulation.

Recommendation 16: Clearer graduated payments regulation

- Enhance graduation of retail payments regulation by clarifying thresholds for regulation by the Australian Securities and Investments Commission and the Australian Prudential Regulation Authority.
- Strengthen consumer protection by mandating the ePayments Code. Introduce a separate prudential regime with two tiers for purchased payment facilities.

Recommendation 17: Interchange fees and customer surcharging

- Improve interchange fee regulation by clarifying thresholds for when they apply, broadening the range of fees and payments they apply to, and lowering interchange fees.
- Improve surcharging regulation by expanding its application and ensuring customers using lower-cost payment methods cannot be over-surcharged by allowing more prescriptive limits on surcharging.

The Government's response to the FSI Report endorsed both these recommendations.

The Review has largely focused on issues relating to recommendation 17. While the Bank's decisions have reflected its obligations under the Payment Systems (Regulation) Act, changes to the standards are all also consistent with the recommendation's objectives. These were to (i) clarify regulation and enhance competitive neutrality between system providers and (ii) improve the efficiency and effectiveness of price signals, and reduce the potential for cross-subsidisation between customer groups and merchant groups.

Consistent with the FSI's recommendation, the Bank's new interchange standards have broadened interchange fee regulation to capture all fees paid to card issuers, including in companion card arrangements. While the new standards have not replaced the weighted-average benchmarks with hard caps, nor expressed the caps as the lesser of a fixed amount and a fixed percentage of transaction values, they include some elements of the recommendations with respect to the level and nature of interchange fee caps. In particular, the debit benchmark has been lowered, and the weighted-average caps have been supplemented by ceilings on individual interchange categories. The Board has chosen not to publish fixed thresholds for when system providers will be regulated, but has signalled some of the factors that would be relevant for decisions to designate additional systems.

Regarding surcharging, the new standard has not incorporated the three-tier model recommended in the FSI Report. However, consistent with the recommendation's aims, the new standard – together with the ACCC's new enforcement powers – will ensure that consumers using a particular payment method are not surcharged an amount greater than the merchant's cost of acceptance for that method.

The first recommendation relates mostly to graduation of regulation, which 'involves providing lower-intensity regulation for new entrants that pose smaller risks to the system — that is, it targets regulation to where it is most needed in the system' (FSI Report, pp 144-5). It also relates mostly to consumer protection and prudential issues that are the responsibility of other regulators, namely ASIC and APRA. In the case of the Bank's competition and efficiency and risk responsibilities, the Bank already has the ability to apply graduated regulation in that the decision to designate and regulate a payment system is not automatic but requires a judgement that it is in the public interest to do so. However, consistent with the Government's response to the FSI and its more recent policies with respect to the 'fintech' industry, the Bank will work with ASIC and APRA to ensure that the regulatory framework is appropriately graduated and encourages innovation. The Bank will also work with the Treasury and ASIC with respect to any regulatory issues involving new payment systems, including digital currencies.

2.3 The Payments System Board's mandate

The responsibilities of the Payments System Board of the Reserve Bank are set out in the *Reserve Bank Act 1959*, which requires the Board to determine the Bank's payments system policy so as to best contribute to: 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 most relevant powers for the current review are those provided to the Reserve Bank under the *Payment Systems (Regulation) Act 1998* (the PSRA). Under the PSRA, the Bank has the power to designate payment systems, and to set standards and access regimes in designated systems. The PSRA also sets out the matters that the Bank must take into account when using these powers.

Under section 18 of the PSRA, the Reserve Bank may impose standards to be complied with by participants in a designated payment system if it considers it to be in the public interest. Section 8 states that in determining whether a particular action is in the public interest, the Bank is to have regard to the desirability of payment systems:

- (a) being (in its opinion):
 - (i) financially safe to use by participants; and
 - (ii) efficient; and
 - (iii) competitive; and
- (b) not (in its opinion) materially causing or contributing to increased risk to the financial system.

The Bank may have regard to other matters that it considers are relevant, but is not required to do so.

2.4 Competition and efficiency in the cards market

This Review has focused on a number of quite different elements of the payments card market in Australia, including: interchange fee levels and regulatory compliance methodologies; the treatment of bank-issued American Express companion cards; transparency of card acceptance costs to merchants; and allowable card surcharges. While quite different in nature, these areas relate in one way or another to the Bank's mandate for competition and efficiency in the payments system.

Consistent with the Bank's earlier analysis, a number of principles underlie the approach taken to the promotion of competition and efficiency in this paper:

- Accurate price signals promote the efficient use of the payments system and the efficient allocation of resources. Distortions to price signals may lead to overuse of some payment methods.
- Relative prices that do not reflect the relative resource costs of different payment systems (i.e. the relative costs to society) are likely to lead to a higher-cost payments system overall.
- In the absence of market failures, effective competition could be relied upon to provide efficient outcomes. Where market failures exist, regulatory options may be appropriate.
- Transparency measures should be preferred to more intrusive regulatory measures where there is confidence that they can be applied effectively.
- Any regulatory intervention should seek to be enforceable, while minimising compliance costs and seeking to be competitively neutral for functionally equivalent systems.

While the Bank's mandate does not include equity considerations, to the extent that improved equity can be achieved through policies that improve competition and efficiency in the payments system, the Bank will seek to do so in the public interest.

Much of the Bank's intervention in the cards market is based on an assessment that there is a market failure that prevents competition from working effectively in this market. In fact, competition between card schemes acts to push prices up, rather than down.

Cards markets are two-sided markets whereby both merchants and cardholders must have an incentive to participate for a system to be successful. However, in a mature cards market like Australia's, many merchants feel they have little choice but to accept a range of cards with little regard to cost, otherwise they will lose business to a competitor. This allows competition between card schemes to focus on the 'issuing side' of the market – that is, competition seeks to influence card issuance by financial institutions, cardholding by individuals and businesses, and the choice of payment method made by the cardholder when making a purchase. Incentives in the system therefore flow towards issuers, in turn funding rewards and interest-free periods for personal cardholders, and reconciliation and expenditure management services for commercial cardholders. Because many merchants feel obliged to accept cards and are relatively insensitive to price, the cost of cardholder benefits can be readily passed through to merchants. Interchange fees (paid from the merchant's bank to the issuer's bank) are central to this incentive framework, placing a floor under the fees that a merchant is charged and supporting the benefits to issuers and cardholders.

The framework put forward in this paper is founded in the Board's earlier decisions to constrain interchange fees through regulation in order to reduce the distorted price signals provided by interchange fees that differed from system to system. It proposes to limit the very high interchange fees that have emerged for some transactions within the existing framework and modestly reduces interchange fee levels overall through a revised compliance framework and a lower debit card benchmark. It also seeks to apply a comparable framework to two products – prepaid cards and American Express companion cards (where a fee similar in form and effect to an interchange fee is paid from American Express to the issuing bank) – that are functionally similar to other, currently regulated products. This will reduce the capacity of interchange fees and interchange-like fees to influence the payment choices of cardholders. The framework also recognises that the economic effect of interchange fees can be replicated through other payments that do not take the exact form of interchange fees and therefore seeks to bring these within regulation.

As noted, approaches that can achieve regulatory objectives through transparency rather than more direct regulation are generally preferred. The principal tool for transparency in card markets is card surcharging. Notionally, concerns about distortions to price signals arising from interchange fees would be reduced if all merchants were to surcharge in a way that accurately reflected the difference in acceptance costs for different methods. Cardholders would make payment choices based on the relative attributes of those methods, rather than in response to interchange fee effects. However, in practice many merchants do not surcharge, either because they feel unable to as their competitors do not, or because they simply do not understand their payment costs. Where they do surcharge, the differentiation between different card products is often limited. In some other cases, particularly where there is an expectation that payments will be made by card, merchants may have an incentive to surcharge more than their acceptance costs so as to keep their advertised prices lower.

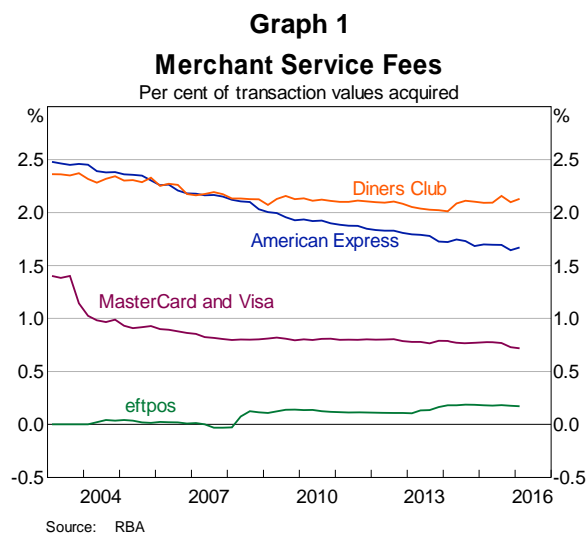
These patterns mean that the Bank has little choice but to rely on direct regulation of interchange fees in order to promote an efficient card payments market. Nonetheless, the Bank's view is that

surcharging continues to improve payment choices and is targeting measures in this Review to improve the effectiveness of surcharging. Together with the Government’s complementary reforms with a consumer protection focus and new enforcement powers for the ACCC, the Bank’s new standard is aimed at preventing excessive surcharging and providing merchants with more easily understandable information on their card acceptance costs.

2.5 The effects of the Bank’s previous reforms

The decisions taken in this Review have been influenced by the experience since the initial round of reforms in the early 2000s. More than a decade on, the Bank’s view remains that the reforms have been in the public interest; they have contributed to a more efficient and competitive payments system. In some cases it is difficult to precisely quantify the effects of the earlier reforms but there is clear evidence of some very positive trends in the payments system over the period of the Bank’s reforms.⁵

The reforms improved access to the cards system, increased transparency and led to more appropriate price signals to consumers. Significantly, the reforms to interchange fees and various measures to strengthen the rights of merchants have combined to place downward pressure on the cost of payment services to merchants. Average merchant service fees for MasterCard and Visa transactions have fallen by 68 basis points relative to their levels prior to the reforms (Graph 1).



The cost savings have been significant – for example, merchants’ payments costs are estimated to have been reduced by \$15 billion relative to the amount they would have paid since 2004 if merchant service fees had remained at pre-reform levels.⁶ To the extent that interchange fees might have risen significantly in the absence of the Bank’s reforms, any estimate of these savings to merchants would be far higher. Indeed, if average merchant service fees on card payments in Australia had instead risen to the levels seen in the absence of interchange regulation in the United States, annual costs to

5 A more detailed analysis of developments in the cards market is provided in the Issues Paper (RBA 2015a).

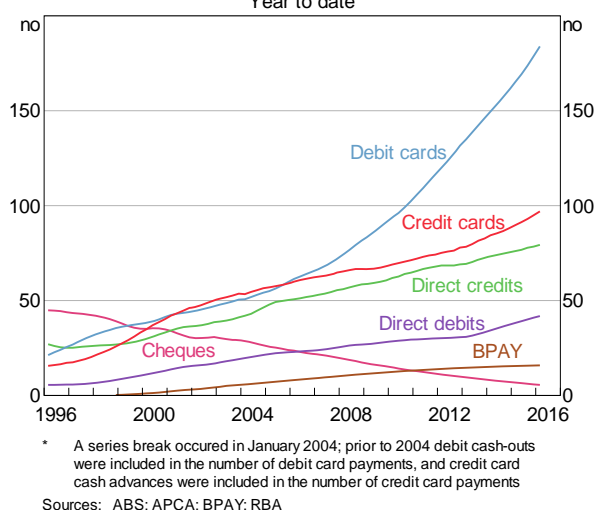
6 This estimate is based on data for schemes’ average merchant service fees with an assumption about the evolution of schemes’ market shares over this period. Similar estimates are obtained if it is assumed that market shares were the same as actually occurred, or if it is assumed that schemes’ market shares remained at their starting levels.

Australian merchants would now be around \$5 billion higher than current levels.⁷ Just as other types of input costs feed through to final prices faced by consumers, the reduction in payment costs resulting from Australia’s reforms will have fed through into lower prices for all consumers, regardless of what payment method they use.

Looking at payment costs more broadly – and including other payment methods in addition to cards – data on aggregate resource costs incurred in producing payments suggest Australia has benefited from a more efficient, lower cost payments system. The results of the Bank’s two comprehensive cost studies indicate that the aggregate resource costs incurred by financial institutions and merchants in accepting consumer payments have fallen from 0.8 per cent of GDP in 2006 to 0.54 per cent of GDP in 2013.⁸ Based on the most recent estimate, it appears that Australia now has a relatively low cost payments system by international standards.

These falls in the cost of payments in Australia have not, however, been associated with any decline in the quality of services offered to end users. The absolute and relative use of debit and credit/charge cards in Australia has continued to increase strongly (Graph 2). The value of card transactions has grown at an average annual rate of 8.7 per cent since 2002, which is above the average annual growth of around 6 per cent in household consumption over this period. The dire predictions of some observers for the future of the cards market at time of the initial reforms have not come to pass. Participants in the cards market have continued to innovate, with the implementation of EMV chip cards, the introduction of contactless payments, and mobile payment technology. In particular, the adoption of contactless payments in Australia has been among the highest in the world.

Graph 2
Non-cash Payments per Capita*
Year to date



7 The calculation takes the number and value of card transactions acquired in Australia and applies US merchant service fees. The US merchant service fee data are from The Nilson Report (2015) for the latest available year (2014) except in the case of debit cards, where pre-Durbin Amendment merchant service fees (2010) are assumed (The Nilson Report 2011). The implied average of merchant service fees for the United States is 1.7 per cent, compared with the actual average for Australia of 0.72 per cent.

8 See Schwartz *et al* (2008) and Stewart *et al* (2014).

3. Interchange Fees and Transparency of Card Payments

3.1 Issues for the Review

This Review has addressed a number of issues relating to the regulation of interchange payments. These include: issues relating to the level of interchange fees; the widening range of interchange fees and implications for the transparency of payment costs; the coverage of the interchange benchmarks (most notably questions concerning prepaid cards and transactions on foreign-issued cards); and the current system for ensuring compliance with the benchmarks. It also raised the issue of whether interchange-like payments to issuers from three-party schemes (notably in the American Express companion card system) should be regulated in the same way as interchange fees in standard four-party business models; this issue is addressed in Chapter 4.

The Issues Paper noted the Board's view that the weighted-average interchange fee benchmarks introduced in the early 2000s have constrained the potential for interchange fees to distort efficient payment choices and have underpinned a fall in the overall resource cost of payments. However, it raised the question of whether the current benchmarks might be inefficiently high; indeed, the Board had considered the possibility of lowering the benchmarks to 0.30 per cent for credit and to 5 cents or even zero for debit when it last reviewed the benchmarks in 2007–08. The FSI Final Report had also concluded that lower interchange fees would improve the efficiency of the payments system. Lower interchange fee caps would likely lead to a reduction in merchant service fees and to product prices being lower than they would otherwise have been for all consumers.

In addition, the Issues Paper noted that average interchange rates, especially for credit cards, have tended to rise to levels significantly above the benchmarks within three-year compliance cycles as schemes and issuers have taken greater advantage of the flexibility offered by the three-year framework. Accordingly, the Bank asked for stakeholder views on moving towards more frequent observance of the benchmarks.

Another development in the schemes' setting of interchange schedules has been the increase in the number of categories and the widening of the range of the rates applying to the categories. The schemes' schedules specify the interchange rate to be paid on a transaction, based on the category of merchant ('strategic', service station etc), the type of card (various types of premium cards, corporate etc) and the nature of the authentication (contactless, SecureCode etc) or value of the transaction. There is a hierarchy of categories, which determines how the merchant, card and transaction categories interact. Typically, the relatively low 'strategic' interchange rates for large merchants take precedence over the interchange category for the type of card, so that the same relatively low rate for strategic merchants applies for all their transactions, including for those using premium cards with high interchange rates. However, merchants who do not have access to strategic or merchant-specific rates will face different rates based on the type of card presented.

One consequence of these developments in interchange schedules is that there are now large differences in the average interchange rates paid on the transactions of strategic or qualifying merchants compared with other merchants. For example, the Bank estimates that the average credit card interchange rate for non-preferred merchants (i.e. those not benefiting from strategic or other preferential rates) was around 55 basis points higher than the interchange rate applying to preferred merchants in the September quarter of 2015. For MasterCard and Visa debit cards, the average interchange rate paid by the non-preferred group of merchants is estimated to have been around 13 cents per transaction higher than the rate applying to the preferred group.⁹ These differences in interchange rates have a corresponding effect on the merchant service fees faced by the two groups. A second consequence of the complex interchange fee schedules is that the non-preferred merchants have little transparency over the cost of particular transactions. In the case of a MasterCard or Visa credit card transaction, the interchange rate is currently around 0.25–0.30 per cent on a standard card but will be 1.80–2.00 per cent if the transaction involves the highest level of premium card. In the case of an average-sized debit transaction, the interchange payment would be around 6 to 8 cents on a standard debit card transaction but around 45–50 cents on a premium or commercial card. Without any visibility over the cost of the particular card used in the transaction, a merchant that wishes to charge to reflect the much higher cost of some cards is unable to do so.

The Bank also considered the types of transactions covered by interchange caps. The Issues Paper noted that there was a degree of ambiguity on interchange arrangements for prepaid cards (which are not explicitly regulated) and that it would be useful to clarify this as part of the Review. Subsequently, consultations with stakeholders have also focused on whether commercial cards should continue to be subject to the same interchange regulation as personal cards. In addition, the Bank has raised the question of whether transactions in Australia on foreign-issued cards should be subject to the same regulation as transactions on domestically issued cards. The Consultation Paper noted both the consideration being given in the European Union to regulation of interchange fees on foreign-issued cards acquired in Europe, as well as the Bank's concern about the possibility of circumvention of Australian regulation by foreign issuance.

3.2 Options presented in consultation

The Consultation Paper outlined a range of potential policy measures to address efficiency and competition concerns and improve the transparency of payment costs for merchants. The Board reached a preliminary view on its preferred options in November and incorporated these in the draft standards published with the Paper.

In the case of the interchange benchmarks, the Board considered a range of options including: leaving the current framework unchanged; removing interchange regulation but introducing other measures to increase the transparency of interchange fees to merchants and strengthen their ability to respond to high-cost cards; retaining a weighted-average framework for the benchmarks, supplemented by a ceiling on individual interchange rates; and reducing the weighted-average benchmarks. For credit, the Board's preliminary view, as reflected in the draft standards, was that it would be appropriate to

⁹ For eftpos, the gap is estimated to be much smaller. The interchange schedule for eftpos Payments Australia Limited (ePAL) is much simpler, with all merchants eligible for an interchange rate of zero on transactions of less than \$15, and then subject to a rate of between zero and 5 cents on larger transactions, depending on whether they qualify for a strategic rate. ePAL does not have 'premium' category cards and therefore does not have any such interchange rates.

retain a 0.50 per cent weighted-average benchmark for interchange and to supplement this with a 0.80 per cent ceiling on individual interchange rates. The Board seriously considered the case for lowering the benchmark to 0.30 per cent but came to the view that supplementing the benchmark with a ceiling would bring about a meaningful reduction in certain interchange fees, particularly when combined with tighter compliance and the inclusion of transactions on foreign-issued cards in the calculation of the weighted-average interchange fee. For debit, the Board's preliminary view was that it would be appropriate to reduce the weighted-average benchmark to 8 cents, supplemented by a cap on individual interchange categories of 15 cents, or 0.20 per cent of the transaction value if the category was specified in percentage terms.

On the coverage of the interchange standards, the Board considered the option of exempting transactions on commercial cards from regulation, but reached the preliminary view that it remained appropriate to continue to include such transactions in all aspects of the regulatory framework. Regarding transactions on foreign-issued cards, the Board decided to consult on a draft standard that included transactions on these cards in the regulatory framework, in terms of both inclusion in the calculation of the weighted-average benchmarks and being subject to the caps on individual interchange categories. For transactions on prepaid cards, the Board considered both retaining the current regulatory approach (where interchange arrangements are expected to be 'broadly in conformity' with debit interchange arrangements), or making it explicit that transactions on these cards were not subject to any interchange regulation. The Board's preliminary preferred option was to formalise the current 'expectation' and make prepaid cards subject to the same interchange regulation as debit cards.

The Board also considered the option of moving from the current three-year compliance cycle to more frequent compliance, to ensure that schemes adhere more closely with regulatory benchmarks. It decided to consult on draft standards that require quarterly compliance with the weighted-average benchmarks. In the event that a scheme's average interchange rates in a quarter were above the benchmark, a reset of interchange schedules within 45 days of the end of the quarter would be required.

3.3 Stakeholder views

Stakeholders expressed a range of views on the appropriate level of interchange caps. End users, such as merchants and consumer groups, were generally supportive of measures to lower interchange fees for both debit and credit, with the growing divergence in interchange rates faced by small and large merchants a particular concern for merchants. Indeed, some end users considered that regulatory caps should be set below the levels proposed in the draft standards; it was observed that the current review presented a 'rare opportunity' to implement substantial reforms to interchange regulation. Consumer groups, for example, suggested that a 0.30 per cent cap on credit interchange fees would be appropriate and argued for significantly lower caps on debit interchange than proposed in the draft standards. The domestic debit scheme, eftpos, supported the proposal for a lower benchmark for debit transactions. A few respondents suggested that interchange fees be eliminated altogether.

Conversely, the international four-party card schemes and financial institutions tended to argue that interchange caps should not be lowered. While in some cases noting their in-principle opposition to any interchange regulation, these stakeholders generally welcomed the Board's preliminary intention to retain a 0.50 per cent weighted-average cap for credit interchange fees. However, most of these

entities expressed the view that the proposed 0.80 per cent cap on individual credit interchange rates was too low and would limit flexibility in the setting of interchange fees.

A particular issue in this context was the view of the international four-party schemes and financial institutions that commercial credit cards should not be subject to the 0.80 per cent cap on individual interchange categories; some argued also that transactions on these cards should not be included in the calculation of the weighted-average for benchmark compliance. These entities argued that four-party commercial credit and charge cards would be unviable or marginally viable with a hard cap of 0.80 per cent. They argued that commercial cards operate differently from personal cards in that the company holding the card is typically charged neither interest nor account fees, so interchange fees constitute a large share of the issuer's source of revenue. While financial institutions had previously reported to staff that rebates are often paid to holders of commercial cards, submissions from banks and the four-party schemes argued that these cases are relatively few and are available only to the largest corporations. Banks and schemes argued that commercial cardholders receive substantial other benefits in the form of reporting tools, integration with expenditure management software and ongoing relationship management, which are costly for the issuer to deliver.

In contrast, submissions from merchants and a consumer group opposed any differential treatment of commercial cards. Several submissions expressed concerns that any difference in regulatory treatment of commercial and consumer cards could result in circumvention. One merchant submission argued that commercial cards are 'must-take' products, difficult to distinguish from consumer cards, and that the benefits to merchants claimed by the schemes and banks were overstated.

On debit, issuers and the international four-party schemes were opposed to a reduction in the weighted-average interchange benchmark and the introduction of a cap on individual debit interchange rates.¹⁰ According to these stakeholders, lower interchange fees would impede innovation in this segment of the market. Some cited the desirability of avoiding a reduction in revenue to the banking sector at a time when there were many industry projects (the New Payments Platform, eftpos' eHub, and online and contactless acceptance of eftpos) underway. Representatives of smaller financial institutions argued that lowering the caps on debit interchange would increase the incentive to issue credit cards rather than debit cards; this could place relatively small issuers at a competitive disadvantage because their product mix is more oriented to debit products. There was a range of views – but limited strongly held opposition – on the question of whether prepaid cards should be explicitly included within the debit card interchange cap.

Merchants and consumer groups were generally supportive of the proposal to bring domestic transactions on foreign-issued cards within the scope of the Bank's interchange regulation, with some pointing to the growing importance of cross-border transactions.

However, a number of submissions from the industry argued that this was a new issue that had not been raised in the Issues Paper and that it should be subject to further consultation with the industry. MasterCard and Visa were strongly opposed to the proposal, suggesting it was 'globally

¹⁰ The Bank has noted that the proposed reduction in the debit benchmark broadly matches the decline in the average value of debit transactions since the debit standard was introduced. A few submissions suggested that the paper had mis-estimated this decline and referred to data that include eftpos transactions. However, the 2006 benchmark of 12 cents was introduced for the multilateral interchange fees of the international systems and was based on data for costs in those systems. Accordingly, the Bank's statement about the fall in transaction values refers to the fall in average transaction size for the international systems (from \$80 in 2006 to \$54 in 2014/15).

unprecedented', could raise serious concerns from Australia's trading partners and that 'international comity' issues may arise. The schemes also suggested that higher interchange rates are needed on cross-border transactions because they are more costly to provide (e.g. because of higher fraud and chargeback risks) and that moving away from a single rate on all international transactions would be computationally burdensome. They argued that reducing the interchange payable to foreign issuers could lead them to implement higher 'decline' rates (especially on card-not-present transactions) and harm for the Australian tourism industry, other exporters and the economy broadly. The schemes also suggested that they would be hurt in issuance decisions in foreign markets if competitors in those jurisdictions were not also subject to interchange regulation on transactions with Australian merchants. The schemes acknowledged the Bank's concern about possible circumvention of domestic interchange caps by offshore issuance into Australia and both have committed to preventing this through their scheme rules. Domestic financial institutions have also expressed concern about the proposal, in part because interchange yields on domestic transactions might have to be lowered to accommodate higher international fees within the weighted-average framework. They also noted the potential for other jurisdictions to reduce interchange fees on Australian-issued cards in response to regulation here. The schemes and some banks have also noted the potential for seasonal and other variations in foreign card transactions to make the proposed quarterly compliance methodology more challenging.

In their submissions, most stakeholders accepted that there was a case for more frequent observance of benchmarks, with end users particularly supportive of tighter compliance. The international four-party schemes and financial institutions were, however, generally opposed to quarterly compliance, mainly on the grounds that more frequent resets of fee schedules would be costly. Some respondents argued for annual compliance, noting, among other things, that seasonal variations or unexpected changes in the pattern of transactions could potentially complicate quarterly compliance. Others commented that requiring a reset within 45 days was a potentially onerous requirement.

A number of submissions expressed concern that American Express proprietary cards would remain outside the regulatory framework. A number of submissions, most notably from the international four-party schemes also argued for the designation and regulation of some other systems, including UnionPay, or for publication of explicit thresholds that would trigger designation.

The Consultation Paper asked respondents to provide views on implementation timeframes for the proposed regulatory changes. End users were typically supportive of accelerated implementation. Some financial institutions and schemes argued for significant time to prepare for the new framework, noting the time that would be required for renegotiation of contracts with partners, internal systems changes, rethinking of product mixes and pricing to customers, and notification of customers. Some merchants indicated that they would require time to adjust to any changes in the surcharging standard.

3.4 The Board's assessment and conclusions

3.4.1 The case for interchange regulation

The Board has carefully considered the views of stakeholders and acknowledges that opinions differ on the role of interchange payments and the case for interchange regulation. However, after extensive consultation, and with the benefit of the evidence since the 2003 reforms, the Board remains of the view that interchange regulation has contributed to a more efficient and competitive payments system. It is noteworthy that following a comprehensive review of the financial system, the

FSI Final Report reached a similar judgement, endorsing the Bank's overall approach to interchange regulation and recommending that the Board consider further reductions in interchange fees. The current Review has also indicated that end users – both consumers and businesses – support the reforms that the Bank has undertaken since 2003. In addition, regulators and competition authorities in a significant number of foreign jurisdictions have implemented similar reforms over the past decade.

Nevertheless, the Board has again considered whether its concerns about the adverse impacts of high interchange fees on the efficiency of the payments system could be mitigated through policy measures that did not involve direct regulation of interchange fees. In principle, it might be possible to seek to strengthen the power of merchants to respond to high interchange rates in their acceptance decisions, for example by ensuring that merchants were provided with real-time information on payments costs and greater ability to respond when high-interchange high-cost cards were presented by cardholders. However, consultation with stakeholders suggests that this would involve significant costs to the industry. In addition, merchants in a range of sectors have indicated that the principle of merchant surcharging for higher-cost means of payment is still not fully accepted, so that they find it very difficult to surcharge to offset the higher cost of particular 'must-take' payment methods. Accordingly, the Board does not consider that it would be possible to step away from interchange regulation and rely on other measures.

3.4.2 The levels of the interchange benchmarks

During the current review, the Board has considered both the case for lowering the interchange benchmarks and changing the nature of the benchmarks from weighted-average caps to hard caps on all interchange fees within a scheme's schedule; the latter now apply in the European Union, with hard caps of 0.20 per cent for debit card transactions and 0.30 per cent for credit card transactions. While the Board has decided to place some constraints on the highest interchange fees that schemes may set (see section 3.4.4), it decided against moving to benchmarks that are hard caps. Accordingly, the draft standards released for consultation in December 2015 continue to specify the benchmarks in weighted-average terms, which will continue to provide schemes with significant flexibility in the setting of interchange fee schedules. The ability for schemes to set higher and lower interchange fee categories may be appropriate in certain situations, for example, where they are seeking to encourage actions such as fraud prevention by issuers, acquirers or merchants.

Regarding the level of the weighted-average caps, the Board accepts that there may be a role for interchange fees in emerging payment systems in encouraging the use of a system by one side of the market or the other. However, the case for significant fees is much weaker as the system becomes well established. The latter conditions clearly apply in Australia; payment cards are now the dominant means of making retail payments, with the relative use of cash declining rapidly (Graph 2). Visa and MasterCard are the two largest schemes and jointly account for around 67 per cent of the value of all card payments (debit, credit and charge). This market share has grown over the past few years, but there has been no tendency for interchange rates in these systems to fall as system volumes have risen and average costs have fallen.

Overall, the current review has not altered the Board's view that there appears to be little justification for significant interchange fee payments in mature card systems. It notes that lower interchange rates would have a number of benefits including: a reduction in the distortion to price signals and therefore an improvement in the efficiency of the payments system; a reduction in payment costs of merchants; reduced cross-subsidisation across consumers paying with different payment methods and downward

pressure on retail prices of goods and services for consumers; reduced need for merchants to consider surcharging of more expensive cards; reduced focus on rewards programs and reduced incentives for the use of payment methods with higher resource costs; a reduction in barriers to entry for potential new methods of payment; and a reduction in the extent to which current arrangements in the card payment systems favour large retailers and higher-income consumers.

The Board also notes that there are instances internationally of card systems that function effectively without interchange fees (and, in fact, with ‘negative’ interchange fees, as was previously the case for the eftpos system) and also recent cases where regulators and card schemes have set lower interchange caps than exist in Australia, including by seeking to align interchange fees with the transactional benefits that merchants derive from card payments (the merchant indifference test).¹¹

In the case of debit cards, the Board has decided to reduce the benchmark to 8 cents.¹² The evolution of the payments system over recent years has seen increasing use of card payments for low-value transactions. This has resulted in the average value of a transaction in the MasterCard and Visa debit card systems falling by around 43 per cent since 2008, which implies that average interchange fees have increased as a percentage of the average debit transaction. A reduction in the weighted-average benchmark could be expected to reduce interchange payments on low-value transactions and may help drive greater acceptance of debit cards for those transactions; currently some merchants do not accept cards for low-value transactions because they consider the transaction costs to be too high. It would also be expected to bring down payment costs for merchants who do not benefit from strategic interchange rates.

In the case of credit cards, the Board considers that there are good arguments that can be made for a lowering of the weighted-average benchmark. Indeed, if there is a case for interchange fees on credit cards to be higher than on debit cards, it is likely to be by only a small amount:

- The existence of significant credit card rewards programs suggests that credit card interchange fees are currently materially higher than is necessary for banks to provide payment cards with credit functionality. The Bank’s 2013 Payments Cost Study shows that – for the average-size transaction for each payment method – the existence of the interest-free period and rewards means that the effective price paid by a cardholder to use a credit card is lower than that for a debit card, even though the resource costs are substantially higher.
- While the existence of rewards and the interest-free period provide a significant incentive for cardholders to use credit cards rather than debit cards, the *payment functions* of debit and credit cards are essentially identical for cardholders and merchants. Thus, it is not surprising, for example, that the work of the European Commission (EC) based on the merchant indifference test suggests interchange fees that are quite similar for debit and credit (and typically relatively close to zero).¹³
- Card schemes and their participants sometimes cite the benefits to merchants and the broader economy from the *credit function* of credit cards, which relaxes credit constraints and enables

11 The merchant indifference test is the proposition that interchange fees be set at a level that results in a cost of card acceptance that makes the typical merchant indifferent between accepting a card payment and other widely used forms of payment. For further details, see Rochet and Tirole (2011) and European Commission (2013).

12 The Board has also determined that the Debit MasterCard system will be formally subject to the standard on debit interchange; previously MasterCard has provided a voluntary undertaking to comply with the Visa Debit standard.

13 See European Commission (2015a).

consumers to bring forward the timing of their purchases. However, simple calculations would suggest this aspect can justify only a small interchange differential relative to debit cards. For example, if credit cards allow 10 per cent of annual credit card spending to occur a year earlier than otherwise (presumably an extreme assumption), if merchants' average profit margin is 10 per cent, and if the relevant interest rate is 6 per cent, the aggregate benefit to merchants of credit cards over debit cards and other payment instruments would be just 0.06 per cent of the annual value of spending on credit cards. This would imply an interchange differential of 6 basis points.

Accordingly, the Board has seriously considered a reduction in the weighted-average benchmark to 0.30 per cent, which would be consistent with the cap implemented for all intra-European transactions in the new EU regulations. On balance, however, it has decided against doing so, partly to reduce the risk of unexpected effects on the competitive balance between three- and four-party schemes or of a significant increase in circumvention efforts. It notes, however, that another element of the new credit card standard, the tighter compliance requirements discussed in section 3.4.8, will result in a reduction in average interchange payments. While the Board's objective in undertaking this Review has been to develop a regulatory framework that will not need to be revisited for some time, it will continue to monitor the appropriateness of the 0.50 per cent benchmark, along with other aspects of the regulatory regime.

3.4.3 Interchange fees and innovation

One of the arguments that some stakeholders have used in the Review is that controls on interchange payments are harmful to innovation in the payments system or will stymie the growth of electronic payments. The Board sees no merits in such arguments for a number of reasons.

First, the evidence of the past decade and a half indicates that there has been very strong growth in card payments in Australia. Contrary to the 2001 submission of one of the international four-party schemes, the cards market did not enter into a 'death spiral' following the introduction of interchange regulation and the removal of no-surcharge rules (MasterCard International 2001). A comparison of the Australian payments system with other markets suggests that there is no shortage of innovation, including in areas such as the adoption of contactless payments, where Australia leads the world. Indeed, a submission on the recent Consultation Paper from the same four-party scheme noted that 'Australia is a leader in electronic payments' (MasterCard Australasia 2016). More broadly, the Bank's regulatory actions do not appear to have made credit card issuing unprofitable; the prevalence of balance transfer offers that offer zero interest for periods of a year or more suggest that financial institutions continue to find the Australian credit card market very attractive notwithstanding the Bank's reforms.

Second, from a conceptual point of view, it is far from clear why a reduction in interchange payments should be viewed as hindering innovation. Innovation in the cards market occurs on both the issuing and acquiring sides. With interchange payments in the international systems flowing always from the acquirer to the issuer, it follows that whether high interchange payments will facilitate or hinder innovation at a particular time will depend on whether the spending that is required at that time is on the issuing or acquiring side.

Third, the Board's view is that a strong case can be made for the Bank's reforms having been supportive of innovation and new entry into the Australian payments system. In particular, as discussed in section 2.4, the nature of competition between mature card systems is for interchange

payments to rise to incentivise financial institutions to issue cards from one scheme rather than another and for issuers to use part of those payments to reward cardholders for using cards from that scheme rather than other payment methods. Caps on interchange payments can limit these dynamics and increase the prospects for new payment methods that could emerge and compete with existing systems, based on their underlying costs and benefits to end users.

3.4.4 The widening of the interchange schedules and effect on transparency of costs to merchants

Consistent with the draft standards in the Consultation Paper, the Board has decided to supplement the weighted-average interchange benchmarks with ceilings on the interchange rates that can be applied to particular interchange categories. For credit, the 0.50 per cent benchmark will be supplemented by a cap of 0.80 per cent on any individual interchange category. For debit, the 8 cents benchmark will be supplemented by caps of 15 cents if the interchange fee for a category is specified as a fixed amount and 0.20 per cent if the fee is specified as a percentage amount. Relative to the current interchange schedules, these ceilings will require reductions in interchange fees on commercial cards and on some premium personal cards. The issues with respect to commercial cards are discussed in section 3.4.5.

These ceilings should result in a significant narrowing in the range of interchange fees faced by those merchants who do not benefit from strategic or preferred rates. The Board considers that this means there is little need to consider facilitating differential surcharging of different credit categories or different debit categories; there is also less of a case for requiring schemes to remove their ‘accept all colours’ rules. In addition, there is likely to be a meaningful reduction in the interchange disadvantage of non-preferred merchants, though this will depend on how the schemes choose to reset their interchange schedules in response to this element (and others) of the changes to the standards. The Bank will be considering publishing data on the average interchange rates paid by preferred and non-preferred merchants.

3.4.5 Commercial cards

In deciding to set the ceiling for all credit card interchange rates at 0.80 per cent, the Board has decided against providing special treatment for commercial cards. The Board was not attracted to the option of leaving commercial cards outside of the weighted-average benchmark framework as this would have implied a significant increase in overall average interchange rates. It considered the possibility of allowing a higher cap for these cards while leaving them in the weighted average but decided against doing so.

The Board is not convinced of the arguments that four-party commercial cards will not be viable for issuers unless a materially higher interchange cap is permitted. First, it notes that while MasterCard and Visa currently have interchange rates for commercial cards that are as high as 1.80 per cent, most of their commercial card transactions are currently at interchange rates that are only moderately above 0.80 per cent. Second, as schemes and issuers have pointed out, commercial cards programs provide significant benefits to cardholders and their corporate purchasing departments, especially in terms of reporting tools, integration with expenditure management software, and ongoing relationship management. Providing this functionality may be costly, and by allowing schemes flexibility to set interchange rates up to 0.80 per cent, it will be possible for schemes to ensure that part of the cost of providing it falls on the merchant. But with the benefits of corporate card programs falling mostly to the cardholding side, it should be expected that much of the cost of these programs

should fall on that side. This may involve the introduction of fees on these cards, the reduction of the interest-free period, or a reduction in rebates in cases where these are paid.

The Board acknowledges that American Express has a significant presence in this sector, and currently does not typically charge annual fees (and may be more able to pay rebates). However, in choosing a card program, corporate purchasing departments can be expected to take account of all the flows associated with card payments, not just issuer charges and rebates. In particular, they will be aware of the higher cost of acceptance of American Express and the likelihood of higher surcharges than for the four-party schemes. Surcharging is more common in merchant sectors where commercial cards are frequently used, and surcharge differentials between three- and four-party schemes are likely to become larger and more apparent with the new regulatory framework, which is likely to reduce the incidence of blended surcharging.

While raised by a number of parties, the decision to leave commercial cards out of the EU interchange framework is not relevant for Australia, because, among other reasons, it occurred in the context of a hard cap of 0.30 per cent on all credit cards.

3.4.6 Transactions on foreign-issued cards

While the Bank's interchange regulation to date has only covered transactions in Australia on domestically issued cards, the Bank proposed in the draft standards to also include transactions in Australia on foreign-issued cards.

This would be consistent with the likely direction of policy in Europe, where the EC has a competition case outstanding against Visa's setting of its 'inter-regional' interchange fees.¹⁴ The EC has also issued a statement of objection with respect to MasterCard's inter-regional interchange fees.¹⁵ In each case, the EC's concerns are that the schemes' cross-border interchange fees are collectively set fees that harm competition between merchants' banks, inflate payment costs for merchants and ultimately increase prices for all consumers, including those who are not paying with high-interchange cards.

The Bank's proposal also reflected concerns about possible circumvention of Australia's interchange regulation if transactions on foreign-issued cards are not subject to the same regulation as transactions on domestically issued cards. Indeed, with the reduction in the highest domestic interchange rates to 0.80 per cent for credit and 0.20 per cent (or 15 cents) for debit, there would be a significant incentive for issuers to take advantage of higher foreign interchange rates (which are typically 1½–2 per cent). This prospect is especially relevant for issuers marketing 'virtual' cards to Australian corporates. The result would be an increase in costs to Australian merchants and prices faced by Australian consumers and businesses.

More fundamentally, as occurs with domestic interchange fees, cross-border interchange fees are set at high levels to influence the issuance decisions of banks and usage decisions of cardholders. The latter decisions in the most part are not the concern of Australian regulators. However, the direct effect on the Australian jurisdiction is the artificially inflated cost of international cards to Australian merchants, with no competitive process available to place downward pressure on those internationally-set fees. Such effects will become more significant as cross-border transactions inevitably increase.

14 See European Commission (2015b).

15 See European Commission (2015c).

The Board welcomes the willingness of the card schemes to prevent circumvention of regulation through cross-border issuance. However, it is not persuaded by the objections of the two large international four-party schemes regarding possible jurisdictional issues. While the Bank is sensitive to the international nature of the card schemes, it has a legislated obligation to promote competition and efficiency in the Australian jurisdiction within the limit of its powers. Domestic regulation in many fields affects foreign parties: the Bank, as with other regulators, is mindful that in addressing issues of domestic concern, foreign entities should not be treated adversely relative to domestic entities. The Board notes that it would be odd if countries were increasingly taking actions to address public policy issues in their domestic payment systems but were somehow unable to address such issues in their jurisdictions simply because they involved foreign entities.

In relation to the schemes' arguments regarding fraud, the Board acknowledges that fraud rates on international transactions – and more specifically on online transactions – are higher than on other transactions and encourages the industry to work to reduce such fraud. However, the Board was not convinced by arguments from the schemes that an extension of the scope of interchange regulation would result in a significant increase in 'decline rates' on transactions at Australian merchants, particularly given the other revenue streams available to issuers on cross-border transactions.¹⁶ Furthermore, to the extent that fraud remains an issue, it was not convinced that an interchange fee that falls on Australian merchants and is passed on to all consumers is an appropriate response; in most cases it is actually the merchant accepting online cross-border transactions that would be expected to bear the cost of chargebacks on fraudulent transactions, with the foreign issuer typically bearing only the administrative costs of dealing with the chargeback.

In summary, the Board's judgement is that there is an efficiency case for considering whether Australian interchange regulation should apply similarly across all types of transactions. However, it notes that the international schemes have committed to use their scheme rules to prevent possible circumvention of domestic interchange caps by offshore issuance. It also notes that transactions on foreign-issued cards currently account for a relatively small share of total card transactions in Australia. Accordingly, for the time being, the Board will not be bringing transactions on foreign-issued cards into our regulatory framework. It will continue to watch developments in this area, including regulatory developments in other jurisdictions, trends in the share of cross-border transactions in overall transactions and whether circumvention of the Bank's standards is occurring.

3.4.7 Prepaid cards

When the Board considered issues relating to prepaid cards in 2006, it determined that it was not necessary to regulate prepaid cards at that time. However, the Board noted its expectations regarding their treatment, including that interchange fees for transactions on these cards would be published and set broadly in conformity with the Standard on interchange fees in the Visa Debit system, and that merchants would not be prevented from surcharging transactions on these cards if they chose.¹⁷

16 Cross-border transactions through the international card systems typically involve charges, in addition to the international interchange fee, that are levied on cardholder and merchant and do not apply to purely domestic transactions. The cardholder will typically pay a foreign transaction fee (around 3 per cent is common, though this is sometimes waived on premium cards) and the merchant will most likely face the international transaction fee that is levied by the scheme on the acquirer.

17 See RBA (2006).

In most respects, prepaid card interchange rates have, to date, been set consistently with the debit card standard, with similar decisions about categories being made by the schemes: both MasterCard and Visa have 'strategic merchant' rates that apply to prepaid transactions at particular merchants and in recent years both have introduced 'premium prepaid' categories with relatively high percentage interchange rates. However, with significant growth in premium prepaid transactions, average prepaid interchange fees for the international schemes have recently been above the 12 cents benchmark applying to debit cards. In addition, the Bank has received queries from a number of payments system participants about the meaning of 'broadly in conformity with', with some parties suggesting that the ambiguity in the wording might contribute to an unlevel playing field. Growth in the use of prepaid cards has meant that the ambiguity associated with the current approach raises more risks than previously and, in addition to the Bank's general concerns about the effect of interchange fees on price signals and incentives, it would be undesirable if the two international schemes were to interpret 'broadly in conformity with' in quite different ways.

The Board's view is that it remains appropriate to treat prepaid cards and debit cards as similar products for the purposes of interchange fee regulation, and that the public interest is best served by formalising the regulatory arrangements, compared with the current approach where the Board has set expectations that may leave room for ambiguity. Different regulatory arrangements would allow scope for regulatory arbitrage, while leaving prepaid cards outside formal regulation appears likely to encourage an upward drift of interchange fees (such a drift in prepaid rates has been apparent since 2013). However, consistent with the general approach to interchange regulation of using a weighted-average benchmark rather than a fixed cap, the drafting of the standard allows for some variation between debit and prepaid rates, subject to ensuring that the overall benchmark is met.

3.4.8 Changes to benchmark compliance

When the benchmarks for credit card interchange fees were introduced in 2003, the Board's aim was to limit the tendency for competition between schemes to drive up interchange fees. By setting the benchmarks in weighted-average terms, the Bank allowed schemes significant flexibility to set different interchange fees for different transactions, some of which could be over the benchmark. Schemes have taken advantage of this, and of the current infrequent compliance arrangements, to develop commercial strategies that encourage issuers to maximise interchange revenue. The result has been that actual average interchange fees have tended to be higher than the regulatory benchmark and have drifted further above the benchmark between the three-yearly compliance points. Accordingly, the benchmark has not represented an effective cap on average interchange fees.

To address this, the draft standards proposed moving to quarterly benchmark compliance. Under this proposal, schemes would be required to reset interchange fee schedules within 45 days of the end of any quarter for which weighted-average interchange fees exceeded the benchmark. Given that frequent resets would be costly for schemes and their members, the Board's expectation was that schemes would set their interchange fee schedules conservatively so that average interchange fees were sufficiently below the benchmark to avoid the need for frequent resets. In addition, the proposed system, with its frequent compliance and ceilings on individual interchange categories, would imply that average interchange fees could not drift far above the benchmark, so any required changes to interchange fee schedules were likely to be more incremental and more easily implemented than under current arrangements.

Consultation responses from the international schemes have referred to the costs of frequent resets, the possibility of compliance breaches due to unexpected changes in transaction patterns, the effect

of seasonality in transaction patterns and the issues involved in resetting schedules within 45 days. For the most part, responses suggested that schemes had not fully digested the Board's desire to ensure that the benchmarks serve as an effective cap on average interchange rates nor taken note of the Board's observation that quarterly compliance does not imply quarterly resets; a straightforward way to avoid frequent resets would be to set their schedules in a manner that does not imply frequent breaches. In discussions with Bank staff about possible alternative annual compliance methodologies, the schemes were not attracted to some form of 'claw-back' mechanism, by which a significant breach of the benchmark in one year would require meeting a lower target in the following year.

Accordingly, the Board has decided on the following compliance methodology. Schemes will be required to keep their rolling four-quarter average interchange fee below the benchmark. At the end of each quarter, the weighted-average interchange fee over the previous four quarters will be calculated. If this is over the benchmark, schemes will be required to reset their rates so that the weighted-average interchange fee under the new schedule, using the transaction mix of the most recent four quarters, would have been below the benchmark.

With compliance being checked at the end of each quarter, the scope – as has occurred under three-yearly compliance and which, in the Board's judgement, might still continue to occur under annual compliance – for average interchange fees to drift significantly above the benchmark should be removed.¹⁸ And by using a four-quarter rolling average interchange fee, the new compliance method will remove any effect of seasonality that would result from compliance based on quarterly averages. Furthermore, schemes will have 60 days, rather than 45 days as proposed in the draft standards, to undertake a reset. In addition, given that at any time they will have full knowledge of their interchange flows and transaction volumes over the prior year, schemes should be better equipped to respond proactively to potential breaches – including to do interchange resets at times that are most suited to their scheduled network releases.

3.4.9 Implementation timeline

In deciding on an implementation timeline, the Board has been mindful of submissions by industry that they would prefer some time to prepare for the new regulatory framework.

Schemes covered by existing regulation will remain subject to the requirements of the current interchange standards until 30 June 2017. The new interchange standards will be effective from 1 July 2017 for compliance with the new interchange benchmarks and the rules on net payments to issuers.

However, there will be elements of the calculations used for compliance that will be backward-looking (as is the case for the current standards). In particular, the first 'reference period' under the new standards will be the period from 1 July 2016 to 30 June 2017. If the weighted average of interchange rates in a scheme over this period is above the relevant benchmark, the scheme will have until 60 days after 30 June 2017 to reset its schedule of interchange rates to comply with the benchmark; i.e. to undertake a reset that, using the new interchange schedule and the transaction mix of the

¹⁸ The Bank has, however, continued to allow a significant degree of flexibility in the way that schemes set their interchange schedules and it might be possible for schemes to set their schedules strategically in ways that – despite the requirement that they would have to reset their schedules every quarter – leave weighted-average interchange rates continually over the benchmark. In the event that schemes were to continue to 'game' the benchmarks, in particular by introducing new, higher interchange categories that initially have zero weights for benchmark purposes following resets, the Board would need to consider a significant tightening of the standards.

previous year, yields a weighted average of interchange rates that is below the benchmark. With the 'rolling quarter' model, the second reference period will be from 1 October 2016 to 30 September 2017 and any reset required would need to take place within 60 days after 30 September 2017.

Schemes will have to certify annually that they have complied with the interchange benchmarks and rules on net payments to issuers (discussed in section 4.4.2). The first certification will be due 31 July 2018 and will relate to the 2017/18 financial year. However, the Board wishes to ensure that the intent of the standard with respect to net payments to issuers is not thwarted by large incentive payments or arrangements that are entered into prior to the new standard taking effect. Accordingly, the calculation of net payments to issuers that becomes effective 1 July 2017 will take into account any incentive payments, rebates or other benefits made between the date that the standards have been registered on the Federal Register of Legislation and 30 June 2017, if those incentives relate to transactions, activity or issuance after 1 July 2017.

Conclusions: Interchange

The weighted-average credit benchmark of 0.50 per cent will be maintained.

The weighted-average interchange fee benchmark for debit cards will be reduced to 8 cents per transaction, which will apply jointly to debit and prepaid cards in each scheme.

Interchange fee caps will be supplemented by ceilings on individual interchange rates: 0.80 per cent for credit; and 15 cents, or 0.20 per cent if the interchange fee is specified in percentage terms, for debit and prepaid.

To prevent interchange fees drifting upwards in the manner that they have previously, compliance with the benchmark will be observed quarterly rather than every three years. A scheme will be required to reset its interchange schedule in the event that its average interchange fee over the previous four-quarter period exceeds the benchmark.

Commercial cards will continue to be included in the benchmark and will be subject to the ceilings above.

Foreign-issued cards acquired in Australia will for the present remain outside the benchmark, in light of commitments from schemes to ensure that the Bank's standards are not circumvented. The Board will take careful note of developments in this area.

The new interchange benchmarks will take effect from 1 July 2017.

4. Competitive Neutrality and Net Payments to Issuers

4.1 Issues for the Review

The Board reviewed issues pertaining to the competitive neutrality of card payments regulation; that is, the implications of regulation applying to some card schemes but not to others. In this regard, a particular focus was on the emergence of American Express ‘companion card’ arrangements subsequent to the Bank’s regulation of interchange fees in four-party card schemes (e.g. Visa and MasterCard) in the early 2000s.¹⁹ The fees paid by American Express to banks that issue these cards are currently not regulated by the Bank, whereas the interchange fees paid in four-party schemes are regulated.

American Express has traditionally operated as a ‘three-party’ scheme whereby it both issues and acquires card transactions; there is therefore no role for interchange fees, and American Express and other three-party schemes have not been subject to the Bank’s interchange regulation. In a companion card arrangement, American Express acquires transactions but partners with financial institutions to issue cards. As part of the arrangement, bilaterally negotiated fees are paid from the scheme to the issuer and, in many respects, these are economically equivalent to the interchange fees paid in traditional four-party arrangements; both are aimed at encouraging banks to issue cards, and support rewards programs and other benefits that promote use by consumers. In particular, some (referred to here as ‘issuer fees’) are related to transaction flows in much the same way as interchange fees.

It has been argued for some time that the different regulatory treatment of payments in companion card arrangements has created incentives for banks to issue companion cards, which, in turn, has contributed to an increase in the market share of American Express. The popularity of companion card arrangements means that average payment costs in the economy are higher than envisaged under the Bank’s weighted-average interchange cap of 0.50 per cent. It has also been argued that, because companion cards have led to American Express cards being more widely held than in the past, fewer merchants are willing to decline American Express. Nonetheless, American Express cards are not as widely accepted as Visa and MasterCard cards and are more often surcharged, or surcharged at a higher rate. This means that American Express is likely to have less market power overall than the other two international card schemes, although this may not be the case in certain industries or segments of the market.

A connected issue is that, in addition to interchange (or interchange-like) fees, both companion card and traditional four-party arrangements may involve the payment of other incentive or marketing fees to issuers. Such fees may incentivise the issuance of particular types of cards. Rather than flowing

¹⁹ Bank-issued American Express cards were initially offered as standalone products. They are now issued as part of a companion arrangement where customers are provided an American Express card as part of a package with a MasterCard or Visa credit card, with both cards accessing the same line of credit.

directly from acquirers, as occurs with interchange fees, these are funded by scheme fees collected by the scheme itself. Schemes can potentially structure non-interchange payments to issuers in ways to circumvent interchange regulation. The Review has therefore considered whether these other payments should also be subject to regulation.

Finally, the Board has considered whether regulation of any other scheme that is not currently designated is warranted.

4.2 Options presented in consultation

The Bank consulted on three approaches to companion cards and associated issues of competitive neutrality:

1. Retaining the current arrangements: companion card issuer fees and other payments to issuers would remain unregulated; interchange fees in four-party schemes would continue to be regulated.
2. Removing regulation of interchange fees for four-party schemes: the four-party schemes would be able to set their interchange fees at their preferred levels to directly compete with American Express companion card arrangements.
3. Regulating issuer fees and other payments to issuers: under this option, payments to issuers of American Express companion credit cards would be regulated. Interchange-like American Express issuer fees and interchange rates in four-party schemes would be subject to the same regulatory benchmarks. Other payments to issuers – in both three- and four-party schemes – would be subject to rules on ‘other net payments’. The implication of the latter is that schemes would not be able to make non-interchange payments to issuers in excess of any payments that they may receive from issuers.

The Board’s preliminary view, expressed in the December Consultation Paper, was that regulating all payments to issuers (the third option) would be in the interest of payments system efficiency and competition. This view was reflected in the draft standards, which also proposed the introduction of a general and objective anti-avoidance provision to minimise the possible circumvention of the Bank’s standards.

With regard to other payment systems, the Consultation Paper noted that some additional systems had been designated in October 2015, in the context of this Review. This raised the question of whether designation and regulation should be considered for other systems. One approach would be to publish thresholds for when a payment system would be subject to regulation, potentially based on market share as suggested in the FSI Final Report.

4.3 Stakeholder views

There were stakeholders on either side of arguments for and against the regulation of interchange-like payments in companion card arrangements. The international four-party schemes argued that if four-party card systems continue to be regulated, all the payments associated with bank-issued companion cards from three-party schemes should be subject to interchange regulation. Consumer groups and most merchants, along with some financial institutions that do not issue companion cards, were supportive of the proposed change in regulation.

American Express argued that the proposed regulation would be detrimental to competition between card schemes because it would benefit the international four-party schemes, which together already account for a large share of the cards market. Some issuers of companion cards focused on the potential disruption to their business models if companion card arrangements were regulated. More generally, it was argued that concerns about ‘competitive neutrality’ had been overstated because American Express had a much smaller share of the cards market than the two largest four-party card schemes; and because American Express cards are not considered ‘must-take’ cards by many merchants and are more often subject to a surcharge.

Several submissions argued that, in addition to companion cards, American Express proprietary cards should be regulated. One argument was that leaving American Express three-party cards outside the regulatory framework would lead to growth in higher-cost schemes and negative outcomes for merchants and consumers. A number of submissions, most notably from the largest four-party schemes, also argued for the designation and regulation of other systems – for example, PayPal, JCB and UnionPay – and/or for the publication of explicit thresholds that would trigger designation.

4.4 The Board’s assessment and conclusions

4.4.1 American Express companion cards and competitive neutrality

The Board considered companion cards when they were first issued in the mid 2000s and again at the time of the 2007–08 review of payments system reforms. It decided against regulation at that time, partly because it believed that imposing ‘interchange’ regulation would have relatively little effect on merchant charges, given that these were negotiated directly between the merchant and American Express as the sole acquirer. Since then, companion cards have become a more significant part of the market, with issuance by two more of the major banks, meaning that shifts in issuer and cardholder behaviour will have a more significant effect on merchant costs. Furthermore, at the time the Bank acknowledged that, to be effective, regulation would need to capture both interchange-like payments and other payments to issuers. The Bank’s view was that regulating the latter payments would be a major step that it was not prepared to take at that time. However, as discussed in section 4.4.2 the Board has reconsidered that view, partly reflecting the implementation of similar restrictions in other jurisdictions.

The Board accepts that the absence of regulation of payments between American Express and its partner banks in companion card arrangements has influenced the development of the market. Over the past decade, issuance of companion cards has grown faster than that of four-party schemes’ cards and of traditional three-party cards. Adjusting for series breaks, the combined share of credit and charge card transactions accounted for by American Express and Diners Club has increased by around three percentage points since the early 2000s and currently stands at around 19 per cent.²⁰ This change largely occurred in two steps, around 2004 and 2009, which coincided with the introduction of bank-issued American Express companion cards by the major Australian banks. While these figures do not separate American Express companion cards from traditional three-party cards, household survey

²⁰ Within these data, a fall in Diners Club’s market share has partly offset an increase in American Express’s market share.

evidence indicates that bank-issued American Express cards have steadily increased their market share since their introduction.²¹

The Board's assessment is that issuer fees in companion card arrangements play a very similar role to interchange fees in influencing payment behaviour. The same can be true of marketing and other payments to issuers from schemes – both three- and four-party. Together, these payments have promoted the issuance by banks of companion cards with comparatively generous cardholder benefits (rewards programs), and provided incentives for cardholders to use these cards ahead of other payment methods. For example, the spending required to earn a reward of a \$100 voucher is typically one-half to two-thirds lower with an American Express companion card than with a MasterCard or Visa card linked to the same account. The Board's assessment therefore is that these payments are distorting payment patterns and promoting the use of products with relatively high resource costs, through means that are very similar to the interchange fees that the Board determined in 2002 that it was in the public interest to regulate.

The Board considered the argument, made by American Express and some other stakeholders, that the bilateral nature of negotiations between issuers and the scheme in companion card arrangements justifies companion cards remaining outside the regulatory perimeter. As discussed above, the Board's assessment is that the flow of fees in companion card arrangements influences behaviour in much the same way as credit card interchange payments, regardless of the manner in which they are negotiated. The Board also noted the argument that companion cards should remain unregulated because American Express has a much smaller market share than MasterCard and Visa. However, American Express companion cards hold a sufficient market share that the effects of interchange-like payments on payment behaviours are material. Further, an expansion in market share of the credit and charge card market and an increased cardholder base appear to be influencing merchant behaviour. Consultation has indicated that a wider cardholder base and acceptance by large retailers, such as major supermarkets, has put pressure on smaller competitors to also accept American Express, and to not surcharge when doing so. Moreover, American Express has a strong presence in particular segments, meaning that American Express is likely to be considered a 'must-take' card among businesses that cater to customers that are more likely to hold American Express cards (e.g. high-end retailers) or in particular sectors of the economy (e.g. travel).

The Board acknowledges that regulation will likely result in a reduction in benefits to holders of companion cards. However this reduction itself represents an improvement in price signals; a cardholder's choice of payment method will be less influenced by differences in the level of payments flowing from schemes and acquirers to issuers, and better reflect the relative attributes of the payment systems themselves. This should result in more efficient payment choices and, based on the Bank's estimates of the relative resource costs of payment systems, a lower-cost payment system overall. The Board notes that regulating companion cards, similar to the ceiling on the highest interchange rates, will also have distributional implications. American Express companion cards, like high-rewards four-party cards, are more commonly held among higher-income individuals. As a result, people on lower incomes are often effectively subsidising those on higher incomes. To the extent that this effect is reduced, equity will be enhanced in the payments system.

Because merchant service fees on all American Express cards (companion and proprietary) are negotiated bilaterally between American Express and merchants, regulation of companion cards may

21 See Ossolinski, Lam and Emery (2014).

not affect merchant service fees directly. Initially, merchants are more likely to see reductions in their payment costs as a result of changes in payment patterns brought about by the improved price signals discussed above. Over time, the competitive forces that have seen American Express merchant service fees decline steadily since the Bank first regulated payment cards can be expected to continue, including as a result of elements of the current regulatory package.

4.4.2 Non-interchange payments to issuers

As discussed above, the Board's view is that placing schemes on an equivalent footing in terms of the relative incentives that can be provided to issuers and cardholders (funded by merchant fees) would require both the application of 'interchange fee' regulation to all schemes and a broadening of the type of payments that are captured in that regulation. The Board's assessment is that, for competitive neutrality and more broadly to prevent possible circumvention of the interchange regulations, it is appropriate for there to be equivalent limits on payments from both three-party and four-party schemes to issuers. The inclusion of a broader range of flows between issuers and schemes is consistent with recent changes to the regulatory framework for credit and debit cards in the European Union and also the regulation on debit card interchange fees in the United States under the Durbin Amendment.

Conclusions: Competitive Neutrality and Net Payments to Issuers

The American Express companion card system that was designated in October 2015 will be subject to the Bank's standard on the setting of credit card interchange fees. Interchange-like issuer fees in companion card arrangements and interchange rates in four-party schemes will be subject to the same regulatory cap.

The standard will introduce limits on non-interchange payments to issuers ('net compensation'), which will apply to all designated card schemes.

4.4.3 Regulation of other payment systems

As noted in chapter 2, the Bank designated the bank-issued American Express companion card system, the Debit MasterCard system and the eftpos, MasterCard and Visa prepaid card systems in October 2015. These decisions were taken in the public interest as the first of a number of steps that the Bank is required to take to exercise its regulatory powers. Decisions in relation to the regulation of these systems are discussed in chapter 3 (interchange) and chapter 5 (surcharging).

The Board also further considered whether other payment systems should be designated, including the case for introducing regulatory thresholds as recommended by some stakeholders and the FSI Final Report. The Consultation Paper noted the Board's preference not to publish explicit numerical thresholds at that stage. Following further consultation, the Board remains of the view that it would not be appropriate to establish this type of automatic trigger for the application of the Bank's power to set standards under the PSRA.²² While automatic thresholds could have the benefit of providing greater clarity to market participants, fixed thresholds are unlikely to be entirely consistent with the public interest requirements of the PSRA. That is, it is the Board's view that judgements about

²² The Bank has implemented thresholds in relation to the regulation of purchased payment facilities (PPFs), as intended by the provisions of the PSRA that relate to PPFs (e.g. section 9 and section 25). However, equivalent provisions do not exist for the powers used by the Bank to regulate card payments.

competition and efficiency involve more complex considerations than just metrics such as market share.

With regard to specific payment systems, the Bank received representations both for and against the regulation of a number of additional (typically smaller) participants. Some argued, for example, that American Express three-party arrangements should be subject to interchange regulation. As has been noted in the past, American Express proprietary cards do not involve the payment of interchange fees (or their equivalent as in companion card arrangements), therefore equivalent regulation is neither possible nor justified. Some parties also noted the potential for three-party schemes to establish outsourced distribution agreements for their proprietary cards, including through banks. The Bank sees this as a normal commercial arrangement that could be put in place with any company with a significant retail distribution capability. Notably, payments under these arrangements are *from* the issuer (in this case the three-party scheme) to the outsourced provider, rather than *to* the issuer to promote issuance and cardholder benefits. The underlying card product remains a three-party product, as discussed above.

While the Board does not see a need to extend interchange fee regulation beyond four-party schemes and companion cards, it nonetheless wishes to ensure that competitive forces apply to the pricing of three-party products to merchants, including through the application of appropriate surcharges. The Board is confident that issues in relation to surcharging and American Express proprietary cards can be effectively dealt with via a voluntary undertaking. As discussed in section 5.4.9, American Express has previously made a voluntary undertaking to remove its no-surcharge rule and has agreed to provide an updated undertaking. In the event that the voluntary undertaking – in combination with the regulation of companion cards and the Government’s ban on excessive surcharging – was not delivering desirable outcomes on surcharging, the Board would reconsider designating the American Express proprietary card system.

More generally, the Board’s expectation is that there would likely be a case for designation if a new four-party card scheme were to undertake any significant domestically focused issuance in the Australian market. This could be relevant in the event that there was significant domestic issuance of UnionPay, a large foreign scheme that is already widely accepted in Australia. In addition, the Board would expect to consider designation of any new companion card arrangements akin to the current American Express model.

5. Excessive Surcharging

5.1 Issues for the Review

The Bank's reforms that took effect in 2003 required schemes to remove no-surcharge rules and rules that prevented merchants from steering consumers to lower-cost payment methods. The ability of merchants to levy surcharges on different types of payment instruments is an important mechanism for promoting the efficient allocation of resources in the payments system. It allows merchants to signal the costs of different payment choices and to pass on these costs to users, aligning end users' private costs more closely to social costs and thereby contributing to a more efficient payments system. The outcome is that merchants are able to set prices for goods and services lower than would be the case if surcharging was prohibited, and the extent to which users of lower-cost payment methods subsidise users of higher-cost methods is reduced. The ability to surcharge also potentially improves merchants' bargaining position in relation to different payment methods, which can help keep downward pressure on merchant service fees and interchange fees.

The ability to surcharge has been a valuable reform, but practices have emerged in some industries where surcharge levels on some transactions appear to be well in excess of merchants' likely acceptance costs. The Bank sought to address these cases with changes to its standard, effective from March 2013, that enabled schemes to limit surcharges to the reasonable cost of acceptance. However, there is wide agreement that the enforcement of this framework has been ineffective. This was highlighted during the recent FSI, which received over 5 000 submissions on the topic as part of a public campaign. Concerns were largely focused on surcharging in the airline and taxi industries. The FSI Final Report cited the complexity of calculating merchants' reasonable cost of acceptance and the associated lack of transparency as factors that have contributed to the limited enforcement of the current regime by schemes and acquirers.

The Bank's March 2015 Issues Paper discussed the issue of excessive surcharging and invited stakeholder views on how to deal with the issue, including on the feasibility of a three-tiered model suggested in the FSI Report. In October 2015, the Government released its response to the FSI, indicating that it would phase in a legislated ban on excessive surcharges, with enforcement to be undertaken by the ACCC. It also indicated its expectations that the Board – through this Review – would provide clarity around what constitutes excessive customer surcharging on card payments. Amendments to the *Competition and Consumer Act 2010* were passed by Parliament on 22 February to give the ACCC enforcement power over surcharges which are above the 'permitted surcharge' defined in a Reserve Bank standard or in a regulation. Accordingly, the implementation of the new legislation, as it relates to card payments, depends on the Bank adopting an amended standard that addresses this definition.

5.2 Options presented in consultation

The December 2015 Consultation Paper canvassed three broad options. The first was to leave the current standard unchanged, an approach which the Paper noted would add considerable complexity

to the ACCC's enforcement of a Government ban on excessive surcharges, given the nature of the draft legislation. A second option would involve removal of regulation, such that schemes would be able to reintroduce the type of no-surcharge rules that were in place prior to the Bank mandating the removal of such rules in 2003. This option would most likely eliminate any instances of excessive surcharging in that it would most likely result in the elimination of *all* surcharging, an outcome which would not be consistent with either the Board's efficiency mandate or the intent of the Government's response to the FSI.

The third option was reflected in the draft standard published in the Consultation Paper. It would entail modifications to the cost of acceptance framework, aimed at preserving the right of merchants to surcharge for high-cost payment methods while ensuring that merchants do not abuse this right by surcharging in excess of their acceptance costs. It would retain the cost of acceptance as the ceiling for surcharges, but would define acceptance costs explicitly and more narrowly. The approach would involve a definition of cost of acceptance focusing on explicit information from acquirers and payment facilitators. The option would require that information on these costs is provided to merchants to enable them to easily calculate their cost of acceptance and thus their permitted surcharge. It would also restate existing obligations for schemes and issuers to make debit and credit cards identifiable visually and electronically, and for schemes and acquirers to make lists of credit and debit Bank Identification Numbers (BINs) available to merchants on request.

5.3 Stakeholder views

While schemes and some financial institutions would prefer to reintroduce no-surcharge rules, the objectives of the proposed changes to the regulation of surcharging received widespread support in submissions, including from consumer groups.²³ However, a number of parties raised concerns about particular elements and a few industries have argued that they may be potentially significantly disadvantaged by the proposed approach.

A number of banks with acquiring businesses expressed concern about the burden that would be placed on them to provide statements to merchants with specific (and easily understood) information on their acceptance costs; this was less of an issue, however, for some other payment service providers with systems that were more conducive to change. Some banks noted that the billing process drew on multiple systems within their organisations (and sometimes from third parties), so that it was not straightforward to provide the scheme-level average cost information proposed by the Bank. Some indicated that they do not currently provide annual statements to merchants, so this would be a significant change. Some suggested that it would be hard to get the internal resources to work on a project to change merchant statements given many other projects that are underway. Given these difficulties, one bank suggested that merchants who wanted information on the cost of different systems should choose an 'interchange-plus' merchant pricing model, which would make the costs fairly explicit. There were different views on the amount of time that acquirers would need to introduce merchant statements with the desired transparency of costs, with some banks suggesting it would take more than 12 months. A number of submissions called for the Bank to work closely with industry on the issue of merchant statements.

Two particular industries – travel agents and event ticketing companies – submitted that they might be significantly disadvantaged by the proposed approach to surcharging. Both are subject to

23 The Bank also received over 1 000 emails from individuals on surcharging as part of its consultation on the Review.

potentially large chargeback risk on cards: this is where a card transaction is reversed, with the cost falling on the merchant, following a complaint to the issuer by the cardholder. Chargeback risk is of particular concern to firms in these two industries because the firm is acting as an agent for the principal (for example, a promoter or venue in the case of the event ticketing industry or an airline or hotel in the case of travel agents). In the event of a chargeback due to fraud by the purchaser or some failure by the principal, the agent may have to refund the total amount of the purchase, even though the booking fee that accrues to the agent is only a small fraction of the total purchase amount.

In the case of the event ticketing industry, other concerns raised included:

- the significant costs to the industry of fraud prevention measures
- the fact that the draft standard would not allow the imposition of a single blended surcharge across several schemes at the average acceptance cost of those different schemes
- the existence of long-term contracts between ticketing firms and venues which included terms relating to the distribution of ticketing revenues, including from payment processing fees
- a more general desire for a significant period of time to implement any required changes to surcharging arrangements.

Submissions from airlines argued for the inclusion of more cost categories – including fraud mitigation costs – associated with card payments, in addition to the merchant service fee, within the definition of allowable costs. One airline also argued that the proposed approach would not achieve a level playing field given that only schemes subject to the Bank’s standard would explicitly be covered in the surcharging framework – the concern here was that an airline might use a foreign acquirer which would not be subject to the Bank’s standard. Airlines also noted the complexity of their booking systems and argued that responding to changes to the surcharging standard would require an extended implementation period.

There was no significant opposition to the proposed treatment of taxis from submissions to the Consultation Paper, namely that surcharging in the taxi industry will largely remain an issue for state taxi regulators.

5.4 The Board’s assessment and conclusions

5.4.1 The importance of the right to surcharge to reflect the cost of payment methods

While the submissions from the international payment schemes have restated their views that surcharging of payment cards should not be allowed, the current review has not changed the Board’s view that the efficiency of the payments system is enhanced by ensuring that merchants have the right to surcharge for more expensive means of payment.

The Board considers that providing merchants with the ability to surcharge payment cards – just as they have the right to surcharge other payment options – has been a valuable reform. It has helped lower the cost of payments by both allowing merchants to encourage cardholders to switch to lower-cost payment methods and enhancing the ability of merchants to negotiate lower card acceptance costs. The Board notes that the option to surcharge is just that – an option – and not necessarily one that many merchants will consider that they need to exercise. Indeed, it might be a good outcome if the combined effects of competitive forces and the regulatory framework are such that there is

sufficient downward pressure on payment costs so that most merchants see little need to surcharge for particular payment methods.

While issues of the disclosure of prices and charges are the responsibility of the ACCC and covered by the Australian Consumer Law (ACL) provisions regarding component and 'drip' pricing, the Board notes also that it is important that any payments surcharge is properly disclosed to consumers. If a particular charge cannot be avoided, then under the ACL it must be built into the up-front price, not added as a surcharge subsequently. For example, if a 'payment processing fee' charged by a ticketing company cannot be avoided in the online environment, the ACL requires that such a fee is already built into the price advertised on an agency's website.²⁴

5.4.2 Surcharging should not be excessive

Consultation with stakeholders has reinforced the Board's view that it is in the public interest that consumers are not surcharged excessively when using cards (or other payment methods). In particular, the efficiency of the payments system is improved where surcharges are not excessive. In the same way that a no-surcharge rule can distort price signals to end users, excessive surcharging of card payments also distorts price signals and may mean that users make fewer card transactions than is optimal given their costs and benefits.

One particular element of stakeholder concern about excessive surcharging has been the use of fixed-dollar surcharging in the airline industry. Given that most of the costs of card acceptance for a merchant vary with transaction values, surcharges of \$7–8 per booking would appear to be well in excess of the cost of accepting cards for low-value domestic airfares, even though they may be well below the cost of acceptance for a high-value airfare such as a cross-country, return business class ticket. Accordingly, the standard that has been adopted by the Board defines the permitted surcharge in terms of the average percentage cost of acceptance. This will require that any surcharge must be set in percentage terms or, if set as a fixed amount, may not exceed the cost of acceptance for the relevant transaction value.

5.4.3 Blended surcharging

The Board has been concerned for some time by the implications of blended surcharging, and this issue was raised by a number of stakeholders during consultation. Where a merchant applies a single surcharge across two systems with different acceptance costs and sets the surcharge at the average acceptance cost of the two, the lower-cost system will be surcharged excessively (i.e. above its acceptance costs). This dulls price signals and does not support efficient payment choices. The amended surcharging standard will preclude the use of blended surcharging where it applies across payment systems (i.e. American Express companion cards, eftpos, MasterCard credit, Debit MasterCard, Visa credit, Visa Debit) and where one or more systems would be surcharged excessively. Merchants may choose to levy the same surcharge on two or more systems in the interests of simplicity, but they will not be able to do so at a rate that is higher than the lowest acceptance cost of those systems.

²⁴ For example, a consumer purchasing a 'face value' \$100 concert ticket online may face two additional fees: a \$6 booking fee and a 1.95 per cent payment processing fee. The ticket cost is typically presented to the consumer as \$101.95 (i.e. including the payment processing fee) and once the number of tickets is selected, the booking fee is added. So a consumer purchasing two tickets will see a price of \$203.90 (2 x \$101.95) plus \$6.00 = \$209.90.

The Board has also decided to include an extra provision relative to the draft standard published in December. In particular the new standard makes it clear that a scheme cannot refuse to provide card services to a merchant because they surcharge or plan to surcharge. This is in effect a no-surcharge rule for new contracts with merchants.

5.4.4 Enforceability and the observability of surchargeable costs

A primary concern in this Review has been to ensure greater enforceability of the Bank's standard. An important element of the improved enforceability of the new surcharging standard will be the new role for the ACCC in enforcing a ban on excessive surcharging. A second element will be that the new standard will require that any costs included in the permitted surcharge are easily observable and verifiable in terms of contracts, statements or invoices. The amended standard will require that merchants are provided with easy-to-understand information on their payment costs. While costs for some payment methods may fluctuate from month to month based on the mix of cards presented, the Bank does not consider that it would be appropriate to require merchants to adjust their surcharges frequently. Accordingly, the revised standard will require that merchants are provided with annual statements that they may use in setting their surcharge over the following year.

5.4.5 The definition of the permitted surcharge

As foreshadowed above, a major issue in consultation with stakeholders was the question of the breadth of the acceptance costs that should be included in the definition of the permitted surcharge.

The current standard and guidance note which became effective in 2013 took an approach that sought to identify all reasonable costs of card acceptance, including some internal costs. Experience with this has indicated that there have been problems in enforcement of limits on excessive surcharges.

Accordingly, the draft standard specified the acceptance costs included in the permitted surcharge for each card system in terms of the merchant service fee for that type of card plus any other card-related fees paid to the merchant's acquirer (or its other main payments provider). These other costs included items such as fees for the rental and maintenance of payment card terminals and scheme fees incurred in processing card payments and passed on by the acquirer. The Board's expectation was that this should be a simple, observable definition that could improve price signals by facilitating enforcement and reducing the scope for merchants to surcharge excessively. The Consultation Paper noted that a comprehensive definition that encompassed a wider range of costs faced by diverse merchants might be conceptually appealing. However, it noted that experience with the current regime suggests that targeting simplicity is likely to lead to an approach to surcharging that is more efficient and enforceable in practice. In particular, costs that are internal to the merchant are not readily observable to a third party and are likely to be difficult to verify in an enforcement context.

Consultation discussions indicated that most stakeholders also place a high priority on a definition for the permissible surcharge that is conducive to effective enforcement where a merchant is surcharging excessively. However, submissions from a few industries highlighted the importance of some additional costs associated with accepting card payments that would not be captured in the cost of acceptance in the draft standard. To a large extent, these costs related to the cost of chargebacks and fraud protection. In particular, as noted above, submissions from the airline industry raised the issue of the costs of fraud prevention. The event ticketing industry also focused on fraud prevention costs, along with the cost of chargebacks resulting from actual fraud, while consultations with travel agents

focused on the costs that were incurred due to the chargeback risk that resulted from ‘forward delivery risk’ (namely that an airline, hotel or other travel provider might fail after cardholder funds had been passed on but before the service had been received).²⁵

While the Board is wary of changes to the draft standard which would make enforcement more difficult, it sees merit in some of the arguments put forward by merchants responding to consultation. For example, the cost of forward delivery risk to travel agents applies only when payments are made via scheme cards and results from scheme rules that require the provision of chargeback protection. The agent would not face this risk if customers paid with a bank transfer or BPAY, for example; in the event of supplier failure, those customers would become unsecured creditors of the supplier. In turn, acquirers typically require agents to post some form of bond or other protection to ensure that cardholders are protected in the event that the agent is unable to repay cardholders.²⁶ This would suggest that where agents face the risk of supplier failure on a particular payment method and take out insurance against that risk, the cost of that insurance should form part of the permitted surcharge.²⁷

The Board also notes that instances of attempted fraud are far more common when customers pay with cards than when they pay with other means such as BPAY or POLi, so merchants often contract for fraud prevention services for card payments. Given that this is a cost associated with card payments, there are good arguments for the inclusion of externally invoiced fraud prevention costs in the permitted surcharge. The Board is wary, however, of allowing the inclusion of all the costs associated with fraud or other chargebacks into card surcharges. It considers that allowing the cost of fraud prevention services and the cost of fraud-related chargeback fees charged by acquirers, but not the actual *ex post* cost of fraud, within the permissible surcharge is appropriate in providing merchants and schemes with incentives to reduce fraud. More generally, the Board encourages the industry to work on reducing fraud in card payments and the development of other payment methods that are less subject to fraud.

Accordingly, following consultations the Board considers it appropriate to make some small changes to the draft standard. These will allow a modest broadening in the costs of acceptance in addition to the average cost of acceptance in annual statements from the merchant’s acquirer or payment facilitator. The five specific items that a merchant could add if they were relevant are: (i) fraud-related chargeback fees paid to the merchant’s acquirer or payment facilitator; fees paid to any other payment services provider for (ii) terminal rental and servicing, (iii) gateway services and (iv) fraud prevention services; as well as (v) any cost of insurance for forward delivery risk on accepting cards. These changes would, for example, allow the inclusion of the cost of purchasing a fraud prevention service from an external provider. They would also allow for cases where merchants choose to source some elements of their card acceptance services (e.g. terminal rental or gateway services) from other parties rather than from their acquirer or payment facilitator. However, for all five of these elements,

25 Agents in the event ticketing industry also pointed to another form of forward delivery risk, namely from the failure of a promoter before a scheduled event; however, the Live Performance Australia Ticketing Code of Practice states that proceeds should be held in trust and only passed on to the promoter after the event has occurred.

26 Alternatively, they may charge agents a higher merchant service fee to cover this risk; in this case, a surcharge based on the merchant service fee will allow agents to surcharge to reflect this risk.

27 Insurance for supplier failure is available to agents, though the market is not well developed and existing products are perceived as being costly for the level of cover provided. Bank staff understand that some other forms of protection against this risk are in development.

the costs must be verified by statements, accounts or invoices from an external provider. Furthermore, they must be costs that apply to cards but not to other payment methods.

One further change from the draft standard is to clarify that the calculation of a merchant's cost of acceptance must take into account any discount or rebate received by the merchant. This will reduce the potential for circumvention of the intent of the surcharging provisions.

5.4.6 Transparency of payments costs

As part of the Review, the Bank has considered whether competition and efficiency in the payments system could be enhanced by improving the transparency of payments cost to merchants. One element is in terms of the information that merchants have about the cost of different payment methods, so as to allow them to make more informed decisions about acceptance and surcharging. This information would also be important for the ACCC in enforcement in cases where merchants may be surcharging excessively. Another element is in terms of whether merchants have visibility of what payment method is being presented – in particular whether a consumer is presenting a debit card or a (typically more costly) credit card.

While a range of stakeholders were supportive of greater transparency about payment costs, the larger acquirers expressed concern about the systems changes that would be needed for them to provide the type of information on monthly and annual costs that would be required under the draft standard. However, the Board continues to take the view that, given the significant differences in the cost of different systems, it is important that merchants receive easily understood information on these costs, including an annual statement that will allow them to make periodic, informed decisions on surcharging. The calculation of this information should in most cases be fairly straightforward for acquirers and payment facilitators – in most cases this would imply providing average costs of acceptance for eftpos, MasterCard credit, Debit MasterCard, Visa credit and Visa Debit.²⁸ However, the Bank notes that systems changes within large financial institutions can take time and is proposing to accommodate the concerns of some respondents in the way it sets implementation dates for the various parts of the reforms (see section 5.4.8).

The Bank is also requiring that the schemes offering both debit and credit cards publish information that allows merchants, acquirers and payment facilitators to distinguish between debit and credit cards. This replaces an existing requirement that this information should be provided on request, with merchants reporting that the current requirement for acquirers to make BINs available on request has not generally been observed. This should enable merchants to surcharge the two types of cards differentially in the online environment if they wish to do so. It may also allow merchants greater flexibility in acceptance decisions in the point-of-sale environment.

As noted in the Consultation Paper, the Bank will not require schemes and acquirers to provide merchants with real-time data on the interchange category and payment cost applying to different cards. The Board notes, however, that the growth of contactless transactions (including the likely growth of transactions using mobile and wearable devices) reduces the ability of merchants to distinguish between debit and (more costly) credit transactions. As this shift occurs, there may be a

28 Where acquirers or facilitators also provide acceptance services for other systems which are not designated, the Board encourages the provision of similar cost information: this will often include UnionPay and JCB. Acceptance and billing of American Express and Diners Club are normally arranged separately by those schemes.

case for bringing interchange payments on credit transactions closer to interchange payments on debit cards.

5.4.7 The taxi industry

The Consultation Paper noted that surcharging in the taxi industry raised difficult issues. Given the greater complexity of the card payments process in the taxi industry and the fact that most aspects of the industry – including taxi fares – are heavily regulated, it suggested that it may be appropriate, for the time being, to leave regulation of surcharging in that industry to state regulators, who may be best placed to assess issues such as the actual cost of providing payment services in taxis and the appropriate rate of return for taxi payment providers.

The Board notes that authorities in five jurisdictions – Victoria, New South Wales, Western Australia, the Australian Capital Territory and South Australia – have now taken decisions to cap surcharges at 5 per cent, which is likely to be closer to the actual cost of providing payments services in taxis than the surcharges of 10 per cent that have previously been typical.²⁹ Accordingly, and consistent with views expressed by a number of parties in consultation, the Board has decided to include a specific provision in the new standard that will have the effect of leaving taxi payments outside of the Bank and ACCC's framework.

5.4.8 Implementation of regulatory changes

Consultation has indicated that a range of stakeholders, most notably consumers, would like to see quick implementation of the new surcharging framework to eliminate excessive surcharging. This would also be consistent with views expressed in Parliament when the Competition and Consumer Amendment (Payment Surcharges) Bill was introduced and enacted. At the same time, the large acquirers have argued that the Bank should provide significant time for the implementation of any requirements for the provision of new statements about payment costs to merchants; in some cases acquirers may provide services to more than 100 000 merchant customers. These two positions present a challenge given that the availability of easy-to-understand statements on payment costs to merchants is a key element of the new RBA/ACCC surcharging framework.

The Board has decided to deal with this challenge by a staged implementation of the new surcharging framework. It notes that concerns about excessive surcharging are most relevant in the case of larger merchants and that these merchants can be presumed to have greater ability to analyse and calculate their payment costs; indeed merchants who are surcharging are likely to already have done such analysis in the current surcharging framework. In contrast, smaller merchants are less likely to surcharge and to surcharge excessively. They often also have a relatively poor understanding of their payment costs, in some cases paradoxically because of the high level of detail on their statements.³⁰ Surcharging decisions for these merchants will benefit from the existence of easy-to-understand data on payment costs.

29 The draft report of the Taxi Industry Inquiry in Victoria (Taxi Industry Inquiry 2012) suggested regulating service fees so they did not exceed the resource cost of providing electronic payment services – i.e. excluding financial flows between processors, operators and networks – and found no evidence that this should exceed 5 per cent of the transaction value.

30 It is not uncommon for merchant statements to include several pages of information about the number and value of transactions for each of the many interchange categories of the international schemes, but to not include summary information on the average costs for transactions within each system.

Accordingly, the Board has decided that the definition of the permitted surcharge will become effective for large merchants on 1 September 2016. Large merchants will be defined as those with consolidated turnover (including that of any related companies) of more than \$25 million in the most recent financial year, or that exceed other thresholds in terms of consolidated assets or number of employees.³¹ While these merchants will not initially be able to rely on the required new statements from acquirers and payment facilitators, they can be expected to have kept records of their payment costs over the previous year or to be able to request duplicates of the relevant statements from providers.

The Board recognises the relatively short implementation period that is being proposed for large merchants. For most merchants – that is, those merchants who are not currently surcharging or are surcharging at levels below the new permitted surcharge levels – the new framework will not require any action. However, in the case of the small number of merchants who may be surcharging at levels that are excessive under the new standard, surcharges will have to be reduced and/or converted to percentage terms relatively quickly. The Board notes, however, that there has been stakeholder concern over excessive surcharging for some time, and that staff discussions with some of the affected companies have indicated a clear awareness of the draft standards and of the amendments to the Competition and Consumer Act that were introduced into Parliament in December 2015 and passed in February.³²

In the case of smaller merchants, the implementation date will be coordinated with the availability of statements from acquirers and payment facilitators on payment costs. The Board has determined an implementation date for the provision of merchant statements of 1 June 2017 which should ensure that all merchants receive statements of their annual average costs for the 2016/17 financial year by July 2017. Accordingly, for merchants with annual turnover of less than \$25 million (and who do not meet the assets or employees thresholds), the permitted surcharge and accompanying ACCC enforcement will become effective on 1 September 2017.

5.4.9 Coverage of different payment systems

The changes to the Bank's surcharging standard have been made to be consistent with the recent amendments to the Competition and Consumer Act, which refers to payments covered by a Reserve Bank standard or a regulation under the Act (see Box B). Given that the Government has not made regulations under the Act, ACCC enforcement powers will initially apply only with respect to surcharging on payments made within the designated payment systems that are covered by the Bank's standard.³³

It would be open to the Board to designate additional payment systems – either card systems or other systems such as the cheque system – and to extend the application of the surcharging standard to

31 The \$25 million threshold is similar to the threshold used by ASIC in distinguishing between large and small proprietary companies: see <http://asic.gov.au/regulatory-resources/financial-reporting-and-audit/preparers-of-financial-reports/are-you-a-large-or-small-proprietary-company/>.

32 The Board notes the existence of long-term contracts in the event ticketing industry which specify the distribution of the various components charged to customers (including the 'payments processing fee') between the ticketing agency and the promoter/venue operator. These contracts typically provide for adjustment of the contractual financial terms in the event of changes to taxation (GST) arrangements, so the parties may be also able to reach agreement on changes to the terms in the event that the new RBA/ACCC surcharging arrangements have any implications for the contractual payments between the parties.

33 The designated systems are the American Express companion card system, the eftpos debit and prepaid systems, and the MasterCard and Visa credit, debit and prepaid systems.

those systems if it considered such measures to be in the public interest. While the Board sees no case for doing so at present, it may be useful to give some sense of the Bank's current thinking with respect to surcharging within other systems.

When the Board implemented its initial reforms, it determined that it was not in the public interest for no-surcharge rules to continue to be applied in the three-party schemes (consistent with its conclusions in relation to four-party scheme rules regarding surcharging), and indicated that it was prepared to set a standard in relation to these schemes. However, a formal standard proved unnecessary, as American Express and Diners Club were prepared to provide undertakings in relation to no-surcharge rules. These undertakings were updated with the changes to the Bank's surcharging standard effective March 2013.

While the American Express companion card system is designated and will be subject to the Bank's surcharging standard, there is no equivalent designation of American Express' proprietary card system. However, American Express has previously made a voluntary undertaking to remove its no-surcharge rule and has indicated it will provide an updated undertaking consistent with the new standard on surcharging. In the absence of a Bank standard covering American Express' proprietary card system, there is no role for ACCC enforcement in cases where consumers using a proprietary card believe they have been surcharged at unreasonably high levels. However, the ACCC will have enforcement powers in relation to surcharging on companion cards and in practice merchants are unlikely to distinguish between companion and proprietary American Express cards in any decisions regarding surcharges. As a consequence, transactions on proprietary cards are unlikely to be surcharged at levels above the permitted surcharge in the Bank's standard. In the event that this does not prove to be the case, it is likely that the Board would consider designating the American Express proprietary card system and making it subject to formal regulation on surcharging.

Diners Club has also indicated it will provide the Bank with an updated undertaking that will ensure that it will not enforce the no-surcharge rule that it applies in other jurisdictions. The Bank will also be seeking new voluntary undertakings regarding the no-surcharge rule applied – albeit inconsistently – by PayPal and other restrictions applied by UnionPay.

Given that none of these three systems are currently designated and subject to the standard on surcharging, there will be no formal or explicit protection for consumers against surcharges that are unreasonably high. However, the Bank's expectation is that merchants who are subject to a framework that caps surcharges in other systems are likely to also follow the 'permitted surcharge' framework in setting any surcharges in these three systems. In addition, in the event that these systems (or any other undesignated systems) were concerned about excessive surcharging on their transactions it would be open to them to include a permitted cost of acceptance in their scheme rules and a requirement that merchants warrant to consumers that any surcharge does not exceed that cost of acceptance. Any excessive surcharge would be both a contractual breach and a misrepresentation on the part of the merchant. Finally, in the event of excessive surcharging on transactions in any of these systems, it will be open to the Bank – if it considers such measures to be in the public interest – to designate the relevant scheme and make it subject to a surcharging standard.

The Bank notes also that its standard, which sets a definition of excessive surcharging for ACCC enforcement, would not facilitate actions in relation to foreign merchants marketing to Australian consumers unless those foreign merchants use Australian acquirers; the Bank's standard applies only to participants in schemes in Australia. To the extent that there were concerns about excessive

surcharging by foreign merchants, it would be open to the Government to consider addressing them via regulation. It is also possible that an Australian merchant that wished to surcharge at excessive levels could engage a foreign acquirer, so that its transactions were not subject to the Bank's standard or to ACCC enforcement regarding excessive surcharges. However, this would require engaging an acquirer in a jurisdiction where surcharging was permitted, where there were no regulations against excessive surcharging, and where payment costs were sufficiently low to make it attractive. It could also expose consumers to international card fees imposed by their banks and could be expected to meet considerable customer resistance. Accordingly, while this scenario is possible, the Bank considers it unlikely, especially given that merchant service fees in Australia are lower than in most other markets, where interchange fees are unregulated. However, to the extent it did occur, it would be open to the Government to address it via regulation.

Box B: *Competition and Consumer Amendment (Payment Surcharges) Act 2016*

In October 2015, the Government released its response to the FSI, announcing that it would provide the ACCC with the power to take action in relation to instances of excessive surcharging. In February 2016, the Parliament passed legislation amending the *Competition and Consumer Act 2010*, enabling the ACCC to issue infringement notices to entities that it considered were surcharging in excess of 'permitted surcharge' levels, with the definition of permitted surcharge to be defined in a Reserve Bank standard or in a regulation.

In determining its approach to surcharging, the Board has taken into account two important factors:

- The need to ensure that any definition of permitted surcharge is consistent with its mandate to promote the public interest (section 2.3).
- The need to define 'permitted surcharge' in a way that can be clearly understood by merchants and is able to be enforced by the ACCC.

Given that the legislation creates obligations for merchants and introduces a new enforcement regime which could potentially involve infringement actions and fines from the ACCC, the Board has been mindful of the need for the definition of permitted surcharge to be as clear as possible. The approach taken sets out a limited list of defined items that can be included in a permitted surcharge, and limits these to cost items that a merchant can readily provide evidence of if required to do so by the ACCC. The scope of included items is narrower than under the current 'reasonable cost of acceptance' and should be able to be both clearly understood by merchants and readily enforceable by the ACCC.

5.4.10 Communication of regulatory changes

The Board considers it important that the surcharging framework is well understood by businesses, consumers and by acquirers and payment facilitators. Businesses should be able to make card acceptance decisions with full information about their payment costs and with confidence about whether their decisions are consistent with the Bank's regulation and the Competition and Consumer Act. Consumers should be able to make purchases with an understanding that any surcharges they face are a reflection of the cost of particular payment instruments. Furthermore, in the event that they believe surcharges may be excessive, they should know the procedures for complaints. It will also be important that acquirers and payment facilitators are aware of the information that must be provided to merchants in statements starting in mid 2017.

Accordingly, the Bank has been working with the ACCC as it prepared drafts of the surcharging standard for consideration by the Board with a focus on ensuring that the new framework will be understandable by stakeholders and enforceable by the ACCC. The Bank has prepared explanatory material for businesses, consumers and the payments industry for release together with this Conclusions Paper and will be available to meet with stakeholders to clarify any issues with the new framework, including on the implementation timeline. The ACCC will engage with consumers and businesses to ensure that the ban is complied with and industry is aware of their obligations under this new framework.

Conclusions: Surcharging

The Bank will introduce a new standard relating to surcharging practices to replace existing standards. The new standard will apply to all designated card schemes. Undertakings by American Express and Diners Club will be updated to reflect the new standard.

Schemes and their participants will continue to be prevented from applying no-surcharge rules.

Consistent with the recent amendments to the Competition and Consumer Act, the standard will define a merchant's 'permitted surcharge' for cards of a scheme. This will be in terms of the merchant's average cost of acceptance of cards of that scheme.

The definition of the cost of acceptance includes merchant service fees and a limited set of other payment costs paid to acquirers, payment facilitators or payment service providers, taking account of any discounts or rebates. Costs that relate also to other payment methods or to the transactions process more generally are not permitted costs of acceptance.

Any surcharge that a merchant chooses to levy must be specified as a percentage of the transaction value or, if set as a fixed amount, must not exceed the cost of acceptance for the relevant transaction value.

If merchants set the same 'blended' surcharge for more than one scheme, they may not do so at a rate that would imply excessive surcharging of any scheme.

Obligations on merchants will be phased in, with surcharging by larger merchants covered from 1 September 2016, while for other merchants the implementation date will be 1 September 2017.

The standard will provide for greater transparency to merchants of the cost of acceptance, with an obligation on acquirers and other payment facilitators to provide easy-to-understand statements on costs to merchants.

Merchants will be able to set surcharges based information from the annual statement from their acquirers or payment facilitators, plus information on costs of certain specific items in contracts, statement or invoices from other external providers.

Transparency will also be enhanced by requiring the publication of BIN lists to enable merchants and their payment service providers to distinguish electronically between cards of different schemes.

Enforcement of the surcharging standard by an independent government agency (the ACCC) will ensure that consumers are not surcharged excessively. Enhanced enforcement will be underpinned by surchargeable costs being restricted to readily observable and easily verified items.

6. Final Standards and Implementation

6.1 New cards regulation standards

The approach to cards regulation outlined in this paper will be implemented through the revocation of several existing standards and the imposition of three new 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

The key elements of these standards are described below.

6.1.1 Standard No.1 of 2016: The Setting of Interchange Fees in the Designated Credit Card Schemes and Net Payments to Issuers

This standard applies to the American Express Companion Card System, the MasterCard Credit Card System and the Visa Credit Card System. It caps the weighted average of interchange fees from 1 July 2017 at 0.500 per cent of transaction value and sets a maximum interchange fee of 0.800 per cent, which cannot be exceeded at any time after 1 July 2017 by any interchange fee in those systems. Fees in the American Express Companion Card System that are functionally equivalent to interchange fees fall within the definition of interchange fees and are subject to these caps. The restrictions do not apply to transactions on foreign-issued cards acquired under these schemes in Australia. Interchange fee rates on a category of card transactions cannot be specified as a range.

The methodology for compliance with the cap for weighted-average interchange fees will change from the current compliance points each third year to a quarterly test of compliance based on rolling annual interchange fee and transaction data. If average interchange fees payable over a period of four quarters exceed 0.500 per cent of transaction value, interchange rates must be reset within 60 days of the end of the quarter to a level that would have prevented fees exceeding the benchmark during the period had they applied. If a scheme changes any interchange rates or categories at any other time, its rates must also be set to a level that would have prevented fees exceeding the benchmark during the preceding four quarters had they applied. The first four quarter period will be the period ending 30 June 2017.

The standard also seeks to prevent circumvention of interchange caps by restricting 'net compensation'. Under these provisions, benefits received by an issuer (excluding interchange fees and some other payments) that have a purpose or effect of promoting the issuance and use of credit cards cannot exceed the payment of benefits by the issuer to the scheme or acquirer in a reporting period. The first reporting period will be from the registration date of the Standard until 30 June 2018. Subsequent reporting periods will be financial years. Benefits that relate to more than one system

must be suitably apportioned and those relating to multiple years may be allocated across those years, up to a limit of 10 years.

Multilateral interchange fee rates must be published and bilaterally negotiated interchange fees must be reported to the Bank. Schemes must certify to the Bank each year that they have been in compliance with the Standard and are required to report information on interchange fees and transactions to the Bank each quarter.

6.1.2 Standard No.2 of 2016: The Setting of Interchange Fees in the Designated Debit and Prepaid Card Schemes and Net Payments to Issuers

This standard applies to the eftpos, MasterCard and Visa debit card and prepaid card systems. It operates in a similar fashion to the credit card standard described above, to cap interchange fees in the debit and prepaid card systems. In this case, weighted-average interchange fees are capped at 8.0 cents per transaction and fees for individual interchange categories cannot exceed 15.0 cents (if levied as a fixed amount) or 0.200 per cent (if levied in percentage terms). The caps on weighted-average interchange fees apply jointly across debit and prepaid cards (referred to as 'scheme pairs'). If the average interchange fee for a scheme pair over four quarters, expressed in cents, exceeds the 8.0 cents benchmark, a reduction in interchange rates would be required within 60 days of the end of the quarter. This methodology implies that weighted-average prepaid interchange fees could exceed the benchmark, provided that weighted-average debit card interchange fees were sufficiently below the benchmark, and vice versa. The other provisions of the standard are similar to those described above for credit cards, including 'net compensation' provisions.

6.1.3 Standard No.3 of 2016: Scheme Rules Relating to Merchant Pricing for Credit, Debit and Prepaid Card Transactions

This standard applies to the MasterCard and Visa credit card systems, the American Express companion card system and the eftpos, MasterCard and Visa debit card and prepaid card systems. Each will be treated as a separate scheme for surcharging purposes, except that debit and prepaid cards will be treated as a 'scheme pair', subject to a single surcharge. The standard prevents the card schemes from imposing no-surcharge rules, but allows them to cap merchant surcharges at the 'permitted surcharge', which is defined in terms of a merchant's cost of acceptance for a particular scheme. The permitted surcharge is also used to determine excessive surcharges under the Competition and Consumer Act.

The 'cost of acceptance' embodied in the 'permitted surcharge' is narrower than the 'reasonable cost of acceptance' measure used in the previous standard (and the associated guidance note). It includes fees paid to the merchant's acquirer or payment facilitator plus fees paid to any other payment services provider for (i) fraud-related chargeback fees paid to the merchant's acquirer or payment facilitator; fees paid to any other payment services provider for (ii) terminal rental and servicing, (iii) gateway services and (iv) fraud prevention services; as well as (v) any cost of insurance for forward delivery risk on accepting cards. Any discounts or rebates received by the merchant are to be taken into account. Costs internal to the merchant are not included.

The permitted surcharge for an individual merchant will be based on an average of its costs over a recent 12-month period as evidenced by contracts, statements or invoices (or, if these are not available for a 12-month period, good faith estimates can be used). A merchant can surcharge each card scheme separately or, if it chooses to apply the same surcharge to more than one scheme, the

permitted surcharge must reflect only the cost of the lowest-cost scheme. Surcharges must be percentage-based or, if expressed as a fixed amount, must not be excessive for any relevant transaction amount.

In order to facilitate greater transparency of permitted surcharges, acquirers (and payment facilitators) will be required to provide to merchants in their regular statements details of the average cost to the merchant of accepting each scheme or scheme pair, along with some component data. The final statement for a financial year must provide the average cost for each scheme over the preceding year. A merchant wishing to rely on a simple statement of acceptance costs will be able to rely on this statement for around a year after it is issued. A merchant wishing to include additional eligible costs would need to be able to provide invoices, contracts or statements to verify them.

Given that many smaller merchants are likely to be reliant on simple acquirer statements to determine acceptance costs, the 'permitted surcharge' measure will not apply to merchants below a size threshold until 1 September 2017, after the new statements have become available. Until that time, card schemes may use their rules to limit surcharges for smaller merchants to the existing 'reasonable cost of acceptance' measure. The permitted surcharge measure will apply to large merchants from 1 September 2016. The threshold for determining whether a merchant is a large merchant will reflect a combination of consolidated gross turnover (above \$25 m), consolidated gross assets (above \$12.5 m) and employees (above 50).

Other measures in the standard include an obligation for acquirers to notify merchants as soon as practicable of the provisions of the new standard; an obligation for debit cards and prepaid cards to be physically identifiable as such (from 1 July 2017 in the case of prepaid cards); and for schemes and acquirers to make available BIN lists that will allow credit, debit and prepaid cards to be electronically identifiable. Card schemes rules will be prevented from making the availability of acquiring services conditional on the merchant's decision to surcharge.

Box C: Key Differences from the Consultation Paper

The Consultation Paper released in December 2015 contained draft standards for consultation. Following stakeholder submissions and consultation with relevant parties, the Board has modified the standards. The main differences between the draft and final standards are as follows:

Interchange:

- Compliance: calculation of a scheme's weighted-average interchange fees is based on a rolling average for the year, measured at the end of each quarter, rather than the average for the most recent quarter only. This ensures that variations in payment values and volumes attributable to quarterly seasonal factors are minimised.
- Coverage of foreign-issued cards acquired in Australia: the draft standards included foreign cards in the benchmark calculation and applied the same ceilings as for domestic transactions. However, at this time the Board has decided not to include these transactions.
- Incorporation of reporting bilateral interchange fee rates to the Reserve Bank in lieu of publication of these rates; schemes with multilateral fees will still be required to publish their rates. The Bank may publish the average of bilateral fees.

Surcharging:

- The elements of cost of acceptance for permitted surcharges are now slightly broader than in the draft standard (although narrower than in the Bank's 2013 Guidance Note on the existing standards) and take account of discounts and rebates.
- The definition of 'permitted surcharge' comes into effect earlier for 'large' merchants (1 September 2016) than it does for other merchants: elements of the existing standard will apply to the latter until 1 September 2017.
- The obligation in relation to BIN lists has been clarified: it now includes an obligation for schemes to publish rather than merely for acquirers to provide to merchants on request.
- The Standard clarifies that a scheme or acquirer would not be able to have as a condition of the contract that the merchant must not surcharge or plan to surcharge: this is equivalent to a no-surcharge rule for new merchants.
- As flagged in the Consultation Paper, the Bank has clarified that surcharging caps in the taxi industry will continue to be applied by state and territory regulators with direct responsibility for taxi regulation: the revised Standard clarifies this to ensure that there is no risk of conflict of law issues arising for state and territory regulation.

Box D: Likely Implications of Regulatory Reforms

In forming its views on a set of reforms to card payments regulation which, in its opinion, are in the public interest, the Board considered the implications for participants in, and end users of, the payments system. This Box summarises the likely effects of the regulatory reforms, considered as a package of measures, on various stakeholders.

Industry participants

- A change in the nature of competition between three- and four-party card schemes is likely. For example, with issuer fees in companion cards subject to the credit card interchange benchmark, there may be a reduction in companion card issuance.
- Reductions in the overall level of interchange payments for debit and credit transactions will flow through into falls in interchange revenue to issuers and falls in four-party merchant service fees. Changes to the debit interchange cap could result in higher card acceptance for low-value transactions.
- A fall in merchant service fees for the four-party schemes is likely to result – as in the Bank’s initial reforms – in downward pressure on three-party merchant service fees. Changes to the surcharging standard will make payment costs more transparent to merchants and may result in reduced blending of surcharges, which will also place downward pressure on three-party merchant service fees.
- Changes to the interchange fee benchmark frameworks and a reduction in merchant service fees will result in less cross-subsidisation/price discrimination between different types of cardholders and consumers, as well as between preferred and non-preferred merchants.
- The caps on maximum interchange rates will bring down interchange fees on commercial cards issued under four-party schemes, which may result in some reduction in rebates or increased fees on these cards.
- Smaller card issuers (e.g. credit unions and building societies) do not generally issue high-interchange, high-rewards cards, and so are likely to be much less affected by caps on the highest interchange rates than the large banks; on the other hand, their card portfolios tend to be weighted more to debit (which will see a larger reduction in interchange) than credit cards.
- Reductions in interchange fees (and, as noted below, the generosity of rewards packages) should reduce the obstacles facing new payment methods in the future.
- Acquirers will be required to make systems changes to provide annual merchant statements and additional information in monthly statements. Schemes will be required to comply with interchange benchmarks each quarter and to reset their schedules in the event of breaches.

Consumers

- Lower merchant service fees can be expected to lead over time to a slightly lower overall level of prices of final goods and services to consumers.
- There will be fewer instances of excessive surcharging, owing to simpler, more transparent surcharging arrangements and enhanced enforceability (including by the ACCC). It is likely that the changes to the interchange standards, the narrower definition of the cost of acceptance and a reduction in blended surcharging will result in a reduction in the frequency of surcharging on some cards.
- The reduction in interchange fees, especially the cap on the highest credit card rates, is likely to result in some reduction in the generosity of rewards programs on some premium cards. It is likely, however, that there will be only limited changes to other elements of the credit card package (e.g. interest rates, interest-free periods). Similarly, the reduction in the high percentage debit/prepaid interchange categories may be likely to result in some reduction in rewards generosity for some of the new debit/prepaid rewards cards. There are unlikely to be other material changes to

arrangements for transaction accounts.

Businesses

- Merchant service fees will fall due to a reduction in interchange payments. There may be additional downward pressure on payment costs to the extent that there is some substitution away from companion cards to lower-cost payment methods.
- The difference between interchange fees on transactions at preferred and non-preferred (mainly smaller) merchants is expected to narrow significantly. Caps on maximum interchange fees will likely benefit small businesses that currently bear most of the cost of corporate and premium consumer cards. For example, for transactions on the highest interchange cards, small merchants on 'interchange-plus' pricing arrangements will see a \$1.20 reduction in merchant service fees on a \$100 transaction using such a card.
- Transparency of payment costs for merchants will be enhanced by changes to the surcharging standard and associated disclosure requirements. The improved disclosure of costs will result in greater merchant awareness of the cost of different payment methods.
- Merchants who currently surcharge for cards will have to ensure that their surcharges do not exceed the cost of acceptance for each payment method. They will have to ensure that any blended surcharges do not result in excessive surcharges for any scheme. Fixed-dollar surcharges will typically be converted to percentage terms.

6.2 Implementation

As outlined in chapters 3 and 5, a number of dates are relevant for the implementation of the new standards:

- 26 May 2016: With registration of the standards on the Federal Register of Legislation, net payments to issuers become potentially included in the calculations regarding net scheme compensation in the Standards on interchange fees. Any payments to issuers that relate to transactions from 1 July 2017 will need to be included in the calculation of 'Net Scheme Compensation'.
- 1 September 2016: the definition of 'permitted surcharge' for large merchants takes effect. Large merchants will need to ensure that they comply with the requirements of the Competition and Consumer Act from this date.
- 1 June 2017: the obligation for acquirers and payment facilitators to provide specific information about the cost of acceptance comes into force. Any statement issued after this date, including annual statements covering the 2016/17 financial year will need to contain cost of acceptance information for merchants.
- 1 July 2017: the new arrangements for interchange fee setting become effective, with the first reference period being 1 July 2016 to 30 June 2017. A scheme whose weighted average of interchange rates is above the benchmark will need to reset rates on or before the day 60 days after the end of that reference period (29 August 2017).
- 1 September 2017: the definition of 'permitted surcharge' takes effect for all other merchants.
- 31 July 2018: the first reporting date for the new regime. Schemes will have to certify to the Bank that their interchange fees were in compliance with the standard for the year ending 30 June 2018.

7. References

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Appendix A: Final Standards

This Appendix sets out the text of the following final standards that were lodged for publication on the Federal Register of Legislation:

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

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**;
- (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;

Benefit means a payment, receipt, rebate, refund, allowance, discount or deduction or a benefit (however named or described) of a similar nature to any of them;

Commencement Date means 1 July 2017;

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);

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;

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

Interchange Fees means:

- (a) for each of the VISA System and the MasterCard System, 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;

Issuer means a participant in a Scheme in Australia that issues Credit Cards of a Scheme to its customers;

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

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

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;

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;

Registration Date means the date on which this Standard is registered in the Federal Register of Legislation;

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, subject to clause 7.3, 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;

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 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 60 days 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 Issuers

5.1 No Issuer which is a 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 an Issuer if the Issuer Receipts of the Issuer for that Scheme over a Reporting Period exceed the Issuer Payments of the Issuer for that Scheme over that Reporting Period.

5.2 For the purpose of this clause 5 and subject to clause 7.3(d):

- (a) subject to paragraphs (c), (d) and (e), **Issuer Receipts** of the Issuer for a Scheme is the total of the Benefits received, directly or indirectly, by the Issuer in relation to Credit Cards of the Scheme or Credit Card Transactions undertaken in the Scheme that have a purpose or likely effect of promoting or incentivising the issuance or use of Credit Cards of the Scheme or of providing or funding incentives to holders of Credit Cards of the Scheme to use those cards, but excluding:
 - (i) Interchange Fees;
 - (ii) payments made by or on behalf of holders of Credit Cards of the Scheme (or holders of the related Credit Card Accounts) to:
 - (A) discharge a liability (whether then due and payable or not) to the Issuer that arose as a result of such a Device being held or used; or
 - (B) create a credit balance in the relevant Credit Card Account; and
 - (iii) any transaction to reverse a Credit Card Transaction or provide a credit or make a chargeback in relation to a Credit Card Transaction.

These Benefits include volume based and transaction specific Benefits such as:

- (i) marketing incentives;
 - (ii) Benefits for meeting or exceeding a specific transaction volume, percentage share or dollar amount of transactions processed; and
 - (iii) signing bonuses;
- (b) subject to paragraphs (c), (d) and (e), **Issuer Payments** of the Issuer for a Scheme is the total amount of all Benefits paid, given or allowed, directly or indirectly, by the Issuer to or in favour of the administrator of the Scheme in Australia or an Acquirer in relation to Credit Cards of the Scheme or Credit Card Transactions undertaken in the Scheme (excluding Interchange Fees and the amount of the Credit Card Transactions paid by the Issuer to the Acquirer to settle obligations arising from the clearing of Credit Card Transactions). These Benefits include:
- (i) Scheme branding fees;
 - (ii) processing fees; and
 - (iii) assessment fees;
- (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 Issuer; 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 Issuer Receipts or Issuer Payments, as applicable;
- (d) one method of apportionment that will be fair and reasonable for the purpose of clause 5.2(c) 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 issued by that Issuer over the Reporting Period as a proportion of the total value of the transactions undertaken in any payment system to which the Benefit relates over the Reporting Period using Devices issued by that Issuer. This does not preclude an apportionment in another way that meets the requirements of clause 5.2(c); and
- (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 on a pro-rata basis based on the number of months in each relevant Reporting Period to which the Benefit relates provided that:
- (i) 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;

- (ii) 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
- (iii) it may not be allocated among more than 10 consecutive Reporting Periods.

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 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.
- 6.2 Each Acquirer and Issuer 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 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 over that Reporting Period in compliance with this Standard.
- 6.4 Each of an administrator of a Scheme in Australia and each Issuer who is a 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, over the most recent Reporting Period, in compliance with clause 5.
- 6.5 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 comes into force on the Commencement Date, but certain provisions in it have a transitional application as set out in this clause 7.
- 7.2 Determination of whether there is an Above Benchmark Reference Period must be made Quarterly in accordance with clause 4.2 from the Commencement Date irrespective of whether the relevant Reference Period commenced before or after the Commencement Date. This means that the first determination under clause 4.2 must be made after the Commencement Date in relation to the Reference Period ending 30 June 2017, even though that Reference Period commenced before the Commencement Date.
- 7.3 For the purposes only of:
- (a) clause 5; and
 - (b) clause 6.4 and clause 7.4 as it relates to clause 6.4:
the:
 - (c) first Reporting Period will be the period from the Registration Date to 30 June 2018; and
 - (d) Net Compensation in relation to an Issuer and a Scheme is to be calculated for that first Reporting Period using only the Issuer Receipts of the Issuer and the Issuer Payments of the Issuer over that first Reporting Period that directly or indirectly relate to issue or use of Credit Cards of the Scheme, or Credit Card Transactions in the Scheme, on or after the Commencement Date.
- 7.4 The first reports and certifications under clauses 6.2, 6.3 and 6.4 must be made by 31 July 2018 in respect of the Reporting Period ending on 30 June 2018.

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;

Benefit means a payment, receipt, rebate, refund, allowance, discount or deduction or a benefit (however named or described) of a similar nature to any of them;

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;

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 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;

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;

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;

Issuer means a participant in a Scheme in Australia that issues Debit Cards or Prepaid Cards of a Scheme (as the case may be) to its customers;

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

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

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;

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);

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;

Registration Date means the date on which this Standard is registered in the Federal Register of Legislation;

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, subject to clause 7.3, 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;

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 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 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.
- 2.6 Each participant in a Scheme must do all things necessary on its part to ensure compliance with this Standard.
- 2.7 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.
- 2.8 This Standard is to be interpreted:
- (a) in accordance with its objective; and
 - (b) by looking beyond form to substance.
- 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, not exceed 15.0 cents; or
 - (ii) 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 60 days 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 60 day period, 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 Issuers

5.1 No Issuer which is a 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 an Issuer if the Issuer Receipts of the Issuer for that Scheme Pair over a Reporting Period exceed the Issuer Payments of the Issuer for that Scheme Pair over that Reporting Period.

5.2 For the purpose of this clause 5 (and subject to clause 7.3(d)):

- (a) subject to paragraphs (c), (d) and (e), **Issuer Receipts** of the Issuer for a Scheme Pair is the total of the Benefits received, directly or indirectly, by the Issuer in relation to any of the Cards of the Schemes in the Scheme Pair or Scheme Pair Transactions that have a purpose, or likely effect of promoting or incentivising the issuance or use of Cards of any Scheme in the Scheme Pair or of providing or funding incentives to holders to use Cards of the Scheme or Scheme Pair, but excluding:
 - (i) Interchange Fees;
 - (ii) payments made by or on behalf of holders of Cards of the Scheme (or holders of the related Card Accounts) to:

- (A) discharge a liability (whether then due and payable or not) to the Issuer that arose as a result of such a Device being held or used; or
- (B) create a credit balance in the relevant Card Account; and
- (iii) any transaction to reverse a Card Transaction or provide a credit or make a chargeback in relation to a Card Transaction.

These Benefits include volume based and transaction specific Benefits such as:

- (i) marketing incentives;
 - (ii) Benefits for meeting or exceeding a specific transaction volume, percentage share or dollar amount of transactions processed; and
 - (iii) signing bonuses;
- (b) subject to paragraphs (c), (d) and (e), **Issuer Payments** of the Issuer for a Scheme Pair is the total amount of all Benefits paid, given or allowed, directly or indirectly, by the Issuer to or in favour of the administrator of a Scheme in the Scheme Pair in Australia or an Acquirer in relation to any of the Cards of the Schemes in the Scheme Pair or Scheme Pair Transactions (excluding Interchange Fees and the amount of the Card Transactions paid by the Issuer to the Acquirer to settle obligations arising from the clearing of Card Transactions). These Benefits include:
- (i) Scheme branding fees;
 - (ii) processing fees; and
 - (iii) assessment fees;
- (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 Issuer; 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 Issuer Receipts or Issuer Payments, as applicable;
- (d) one method of apportionment that will be fair and reasonable for the purpose of clause 5.2(c) 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 issued by that Issuer over the Reporting Period as a proportion of the total value of the transactions undertaken in any payment system to which the Benefit relates over the Reporting Period using Devices issued by that Issuer. This does not preclude an apportionment in another way that meets the requirements of clause 5.2(c); and
- (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 on a pro-rata basis based on the number of months in each relevant Reporting Period to which the Benefit relates provided that:

- (i) 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;
- (ii) 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
- (iii) it may not be allocated among more than 10 consecutive Reporting Periods.

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 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.

6.2 Each Acquirer and Issuer 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 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 over that Reporting Period in compliance with this Standard.

6.4 Each of an administrator of a Scheme in Australia and each Issuer who is a 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, over the most recent Reporting Period, in compliance with clause 5.

6.5 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 comes into force on the Commencement Date, but certain provisions in it have a transitional application as set out in this clause 7.
- 7.2 Determination of whether there is an Above Benchmark Reference Period must be made Quarterly in accordance with clause 4.2 from the Commencement Date irrespective of whether the relevant Reference Period commenced before or after the Commencement Date. This means that the first determination under clause 4.2 must be made after the Commencement Date in relation to the Reference Period ending 30 June 2017, even though that Reference Period commenced before the Commencement Date.
- 7.3 For the purposes only of:
 - (a) clause 5; and
 - (b) clause 6.4 and clause 7.4 as it relates to clause 6.4:
the:
 - (c) first Reporting Period will be the period from the Registration Date to 30 June 2018; and
 - (d) Net Compensation in relation to an Issuer and a Scheme Pair is to be calculated for that first Reporting Period using only the Issuer Receipts of the Issuer and the Issuer Payments of the Issuer over that first Reporting Period that directly or indirectly relate to issue or use of Cards of the Schemes in the Scheme Pair, or Scheme Pair Transactions, on or after the Commencement Date.
- 7.4 The first reports and certifications under clauses 6.2, 6.3 and 6.4 must be made by 31 July 2018 in respect of the Reporting Period ending on 30 June 2018.

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) 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) 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) 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) 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) 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

- (i) 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 5;

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 5.1(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 4.2;

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 7.2(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 4.1 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 5, **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 4.2(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 5.1, 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 5.2 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 6.2:
- (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 7.3, 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 7.3, 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 7.1 or 7.2 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 7.1 or 7.2 (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 7.1 and 7.2 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 7.1 or 7.2 (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 7.1 or 7.2 (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 8.1, 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 9.
- 9.2 Without limiting clause 9.1, the provisions of clauses 3, 4 and 5 will apply in relation to a Merchant that is a Large Merchant on and from the Commencement Date.
- 9.3 The provisions of clauses 3, 4 and 5 will not apply in relation to a Merchant that is not a Large Merchant until 1 September 2017, on which date clauses 3, 4 and 5 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
 - (ii) 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 7.2 and 7.3 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 7.2(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 7.2(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.