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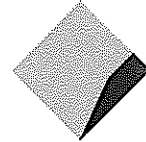
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Government and Industry Affairs
Group Corporate Affairs

20 June 2013

Mr Colin Neave
Chairman
Commonwealth Consumer Affairs Advisory Council
c/- Competition and Consumer Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600



Refer: Mark Frost, Policy Analyst

By Email to: CCAAC@treasury.gov.au

Dear Mr Neave,

CCAAC Study – Credit Card Surcharges and Transaction Fees

I refer to your letter of 3 June 2013 (and email of the same date) in relation to the Commonwealth Consumer Affairs Advisory Council (CCAAC – the Council) study into credit card surcharges and transaction fees.

The Commonwealth Bank (the Bank) appreciates the opportunity to provide a brief submission on the matters being considered as part of this study.

Before turning to the specific questions posed in your letter of 3 June, it is worthwhile to recap on the lengthy consultation undertaken by the Payments System Board of the Reserve Bank of Australia (RBA) in relation to credit card surcharging. Without going into the detail of the RBA conclusions, we do wish to highlight the findings, details of which can be found at:

- June 2012: <http://www.rba.gov.au/payments-system/reforms/cards/201206-var-surcharging-stnds-fin-ref-ris/index.html>; and
- November 2012: <http://www.rba.gov.au/media-releases/2012/mr-12-34.html>.

Of more particular relevance to this submission, however, are the Bank's numerous contributions to the RBA consultation process on card surcharging, evidencing the seriousness with which the Bank approaches such matters. Our submissions are all on the public record and can be found at:

- July 2011: <http://www.rba.gov.au/payments-system/reforms/submissions-card-surcharging/cba.pdf>;
- February 2012: <http://www.rba.gov.au/payments-system/reforms/submissions-var-surcharging-stnds/cba.pdf>;
- July 2012: <http://www.rba.gov.au/payments-system/reforms/submissions-draft-guidance-note-var-surcharging-stnds/cba-06072012.pdf>; and

- September 2012: <http://www.rba.gov.au/payments-system/reforms/submissions/revised-draft-guidance-note-for-the-varied-surcharging-standards/cba-11092012.pdf>.

These submissions provide background and context that we believe the Council will find useful. We would be happy to meet with you or the Council at any time should you wish to discuss any of the matters addressed in the Bank's prior submissions to the RBA.

Turning now to the questions posed in your letter, and addressing each seriatim:

Recent changes to the surcharging standards

What incentives (economic or otherwise) regulate the behaviour of card schemes, acquirers and merchants with respect to the application and enforcement of card scheme rules regarding credit card surcharges?

This is a question best addressed by the various credit card schemes, as owners of relevant rules and operating procedures. An important part of those scheme rules includes compliance requirements with associated sanction regimes. RBA Standards are also relevant and are generally reflected into card scheme rules. Credit card schemes are best placed to provide details of compliance requirements.

At its most basic level, credit card payments systems are based on networks comprising of co-operative providers and their end-user customers. By and large, the co-operation necessary within networks is respected by payments providers (financial institutions and card schemes). In our experience, this respect is reflected in an almost universal regard for the prevailing scheme rules and regulatory fiat. In fact, within the industry, participants are concerned not just about the rules, but also for their relationship with regulators and how actions undertaken by a participant may be assessed by a regulator.

Card acceptance is almost essential amongst Australian retailers – based on the known spending preferences of their customers. This translates to an extremely large number of card accepting merchants. By and large, there are very few merchants who test the rules of card acceptance. However, acquirers do have some ability to correct the behaviour, without terminating the contract, of a merchant who is determined to continue its behaviours – and before a card scheme were to apply sanctions.

To the extent that card scheme rules limit credit card surcharges to the reasonable cost of card acceptance:

- *what processes have been put in place by card schemes, acquirers and merchants to ensure that credit card surcharges are limited to the reasonable cost of card acceptance (including with reference to guidance issued by the Reserve Bank of Australia); and*
- *how are such rules enforced and are there any circumstances where these rules would be selectively enforced (i.e. where the rules would be more aggressively enforced for some merchants and not enforced for others)?*

Further to the above answer, credit card schemes have instituted rules and processes designed to replicate the requirements articulated by the RBA. Details of those processes and the associated enforcement regime are best described by the relevant credit card schemes. It would be most unusual for a credit card scheme to apply a selective approach to merchant enforcement.

It is important to remember that under a traditional “four party” credit card scheme model (cardholder, issuing financial institution, merchant, and merchant financial institution or acquirer), credit card schemes only hold contractual, membership, arrangements with the card issuer or transaction acquirer – not the cardholder or the merchant. Thus, enforcement can only be applied to the relevant financial institution who then holds a subsequent contractual relationship with the cardholder and / or merchant.

It is not possible for an acquirer to continually monitor the surcharging practices of all of its merchant clients – and nor is it warranted. This is a point that is apparent in the above referenced submissions that we have previously lodged with the RBA. As stated above, in our opinion, the vast majority of merchants abide by the rules.

To the extent that card scheme rules do not limit credit card surcharges to the reasonable cost of card acceptance: – what processes, if any, have been put in place, or are being prepared by card schemes, to adopt rules to limit credit card surcharges to the reasonable cost of card acceptance?

As indicated above, card scheme rules are now largely consistent with the reasonable cost of card acceptance approach as articulated by the RBA. Details of any further requirements – in place or contemplated – are best addressed directly with the relevant card schemes.

What mechanisms are available for consumers to report credit card surcharges that appear excessive and that may be in breach of card scheme rules?

In the first instance, cardholders are encouraged to register any complaint with the potentially offending merchant, seeking immediate amendment. Alternatively, a cardholder can contact the affected card scheme (eg via the email address on the Visa web site - surchargingfeedback@visa.com).

The Australian Securities and Investments Commission (ASIC), who is charged with ensuring that financial markets are fair and transparent and supported by confident and informed investors and consumers, is also available as an avenue for cardholder complaint.

On a related aspect, the Bank has previously suggested to the RBA (9 February 2012) that we believe that monitoring of *“merchant compliance with the RBA’s modified Standards and / or any associated Scheme rules on an exceptions basis. This would mean only those merchants who are suspected, with reason, to be non-compliant or applying an excessive level of surcharging, would be required to demonstrate their compliance. This absolves the large majority of surcharging merchants, who, it would seem, do not surcharge in excess of reasonable costs, from any unnecessary burden.*

The organisation charged with investigating the compliance of merchants should be independent, qualified and respected and one with whom the merchant needs to be confident in sharing confidential, and commercially sensitive, data if required. On this basis, acquirers should be excluded because they have an interest in maintaining their business relationship with their merchant customer and are also unlikely to be aware of all costs incurred by the merchant. Card Schemes should also be excluded from this role because they have a vested interest in discouraging merchant surcharging and are similarly not privy to commercial arrangements that may be in place between the merchant and their acquirer (as well as being unaware of other, reasonable, costs that the merchant may incur in accepting card payments).

We believe that there are a number of suitable candidates that are well placed to monitor merchant compliance with surcharging Standards and we again take this opportunity to remind the RBA of the Australian Securities and Investments Commission’s (ASIC) responsibilities with regard to ensuring that financial markets are fair and transparent and supported by confident and informed investors and consumers. ASIC already exercises oversight over surcharging practices and seems well placed to provide additional monitoring as the need arises.”

Surcharges, fees and operational requirements

What factors (including with regards to legal, marketing and accounting considerations) do businesses consider when applying separate fees or surcharges to recover particular costs associated with providing the good or service?

Details as to the factors considered by a business in determining fees, or indeed any other prices or charges, are a matter for the business concerned and will vary between businesses.

In November 2012, the RBA published a "Guidance Note" addressing a series of costs that might usefully be considered by a business in assessing the level of surcharge that it might apply if it so chose. The Note lists some high level cost categories that might be included in addition to the merchant service fee that the merchant pays its financial services provider. The Note is available at <http://www.rba.gov.au/payments-system/reforms/cards/201211-var-surcharging-stnds-guidance/guidance-note.html> .

To the extent that surcharges or fees are applied that appear to consumers to go beyond the reasonable cost of card acceptance or other transaction costs:

- are there any factors that could explain why a credit card surcharge or transaction fee recovering reasonable costs appears excessive; and
- are there any circumstances where it may be necessary or appropriate to apply a surcharge or fee for purposes beyond the recovery of costs?

The Bank has previously submitted to the RBA the principle that any surcharge should be reflective of costs and not a profit line item in its own right. Accordingly, and bearing in mind the contents of the RBA Guidance Note, we believe that it would be difficult to justify excessive surcharging, but again, these are matters for a business to determine within the constraints imposed by the market within which it operates.

We do however emphasise that the list of additional costs relevant to each merchant will vary between merchants – some merchants in certain industries may incur higher costs associated with the perceived riskiness of the industry within which they operate (such as risks associated with the delivery of a good or service some considerable time after payment for that good or service). The airline industry is a good example of this. Similarly, some industries warrant a higher level of investment in fraud prevention, so it is clear that assessment of what constitutes "excessive" cannot always be readily assessed and needs to be considered on a case by case basis.

Importantly, the RBA Guidelines explicitly acknowledge the right of merchants to "recover their card acceptance costs through a surcharge ...". However, applicable costs will vary between merchants.

What factors do businesses consider when applying and determining credit card surcharges and how do businesses determine how the surcharge should be applied (for example, as a percentage of the transaction or as a fixed amount)?

Details as to the factors considered by a business in determining fees, or indeed any other prices or charges, are a matter for the business concerned and will vary between businesses. In addition to cost recovery, a merchant will need to consider customer impact and such factors as ease of implementation, and transparency. An ad-valorem vs fixed fee would likely take into consideration the nature of the input costs being recovered.

Aside from credit card fees and transaction surcharges, what other methods can be used to manage the operational needs of businesses offering credit card payment methods (for example, by imposing \$10 minimum amounts for credit card purchases).

This is a matter best addressed by the businesses concerned but would need to consider working capital management solutions available from many financial services providers, along with an assessment of alternative methods of cost recovery such as incorporating such costs in the broader business cost base which is in turn reflected in

the general level of prices charged. Equity aspects of cross subsidisation are a matter for the business concerned.

Transparency, disclosure and consumer law

How do merchants ensure that consumers are informed about the application of credit card surcharges or transaction fees?

This is a matter best addressed by the businesses concerned.

The Bank has previously argued to the RBA that *"We believe that any surcharging applied by merchants must be transparent at the point of sale (and prior to "check out" in an on-line environment). Transparency, we believe, is important in encouraging competitive responses. We believe that this requirement could be more effectively adopted and enforced than is currently the case."* (19 July 2011)

The ASIC web site advises cardholders that:

*"Merchants may use a variety of means to inform you if they are charging a credit card fee, including prominent in-store and point-of-sale signage, and prominent messages on bills and the internet. Ideally, they may even let you know through their advertisements and promotional tools. From 1 January 2003 you should be on the look out for such notices. Our **advice to merchants about informing consumers about any credit card fees** is available on this website (www.asic.gov.au) or through our Infoline on 1300 300 630." (<http://www.asic.gov.au/asic/asic.nsf/byheadline/02%2F457+Consumer+tips+about+credit+card+fees+charged+by+merchants?openDocument>)*

What approaches could be taken to improve the transparency of credit card surcharges and transaction fees that:

- are a significant component of the total cost such that they have the potential to mislead consumers about the true cost of a good or service;*
- are applied to certain payment methods or across a single transaction such that it cannot be quantified as part of the unit price of a good or service; and*
- cannot be easily avoided where practical surcharge and fee-free payment methods are not available?*

As noted above, the Bank believes that transparency is important but also an area that presents room for improvement. We have previously argued that surcharging applied by merchants must be transparent at the point of sale (and prior to "check out" in an on-line environment). Greater disclosure would aid market efficiency and aid consumer education and awareness.

We note that misleading consumers is likely to prove anti-competitive and thus likely to contravene competition related legislation.

The issue of a surcharge being applied to certain payment methods or across a single transaction such that it cannot be quantified as part of the unit price of a good or service is, we believe, relatively isolated and generally applies to flat rate surcharging. We don't believe that this is a significant issue at present.

Australian merchants are well served by a wide range of options for accepting payments and should remain free to determine what methods of payment they accept. In the majority of cases, alternative means of (surcharge free) payment are available. Even in cases of merchants such as online businesses – relying heavily upon card payments – alternative options are often available.

Importantly, financial services innovation is strong within Australia and it is likely that non card methods of payment for use in an online shopping environment will evolve in the

near future. This is a trait of a competitive and innovative market and will exert pressure on those products that continue to be subject to surcharging.

Are there any circumstances where credit card surcharges and transaction fees:

– cannot be displayed prior to the final stages of a checkout or an online payment form (for example at the final stage where consumers are required to confirm that they want to purchase the goods or services).

– cannot be made known to consumers in a manner such that they are of equal prominence to the purchase price, including with respect to the time at which it is disclosed and its visibility.

Is there a need for additional protections to ensure the transparency of credit card surcharges or fees?

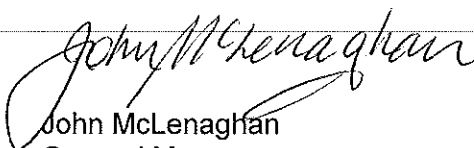
We believe that circumstances of an inability to disclose a surcharge would be rare, but this question is best addressed by the business concerned.

As we note above, we believe that transparency at checkout could be more effectively adopted and enforced than is currently the case but we do not consider this to be a widespread problem.

Finally, we have previously suggested to the RBA that while this discussion *“has concentrated on surcharging as it relates to acceptance of card based payments, we believe it would be wrong to overlook merchant acceptance costs associated with other payment channels such as cash or cheques. The costs of accepting such payments are frequently “hidden” and less transparent than for card payments, yet no less real, and we urge greater public discussion around such costs. The Reserve Bank’ “Strategic Review of Innovation in the Payments System” documents released subsequent to the surcharging Consultation Document, provides some additional information in this regard, but we remain concerned that a focus on card acceptance costs in isolation (and, indeed, surcharging thereof), may inadvertently diminish the attraction of card acceptance vis-a-vis these other, less efficient, channels. The Reserve Bank has frequently spoken of the importance of efficiency in payments, and focussing on surcharging for card acceptance in isolation from substitute payment instruments may mitigate against this goal. We encourage greater public debate, with supporting data and analytics, around this issue and we believe that the Reserve Bank is well placed to contribute to, and shape, this debate.”* (19 July 2011). Council’s assistance in promoting this further aspect of the debate would be welcome.

Thank you again for the opportunity to comment on these matters. We of course remain available to discuss these comments with you at any time and to that end ask that you contact either the writer on mclenajo@cba.com.au or (02) 9118-7686, or alternatively Stuart Woodward (General Manager, Representation, Cards, Payments and Retail Strategy) is well placed to assist and can be reached on woodward@cba.com.au or (02) 9118-6545.

Yours sincerely



John McLenaghan
General Manager
Government and Industry Affairs