



**Submission to the Reserve
Bank of Australia.**

**AFTA's response to the
Review of card payments
regulation Consultation
Paper December 2015.**

February 2016

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Executive Summary

The Australian Federation of Travel Agents (AFTA) provided initial feedback to the Reserve Bank of Australia (RBA) in April 2015 and this Submission should be read in conjunction with that Submission.

AFTA has welcomed the RBA's and Commonwealth Government's commitment to the continuation of surcharging however is concerned that the narrowing of the cost of acceptance will increase the costs for merchants such as travel agents. AFTA notes that the December 2015 Discussion Paper details the intention to remove blended surcharging. This approach will have a significant detrimental effect for intermediaries such as travel agents and AFTA has recommended a possible addition (Attachment 1) to the proposed draft standard.

Of the eight Reform Options AFTA is providing comment on five:

- a. Reform option A – Companion cards, *(Note)*
- b. Reform option B – Interchange fees, *(in-principle support)*
- c. Reform option C – International cards, *(Supportive)*
- d. Reform option D – Prepaid cards, *(Supportive)*
- e. Reform Option G – Surcharging, *(Not supportive)*

Of the five comments, AFTA has noted one, supportive of two, in-principle support of one and not supportive of one Reform Option. AFTA currently does not support the implementation of Reform Option G as it does not allow intermediaries the opportunity to mitigate risks which are solely associated with a consumer choice to use a credit card. In Comment 1, AFTA details that the changes to the surcharging arrangements currently suggested in option 3, of Reform Option G, does not provide the scope for merchants to include Forward Delivery Risk (FDR) and subsequent no fault third party chargeback as a cost of acceptance.

The RBA notes that, intermediaries are the only industry segment that has the exposure to 3rd party no fault charge back risk which only occurs where an agent purchases the product or service on behalf of a consumer. Positively the RBA have sought possible solutions to solve this issue. In response AFTA has developed a Framework to be inserted into the final regulation (Attachment 1). The Framework provides variables for consideration by the RBA and would allow merchants to use a variety of techniques to mitigate a merchants FDR. These techniques would be evaluated by the RBA and enforceable by the Australian Competition and Consumer Commission (ACCC) and provides consumers accurate price signals of their payment choice.

As detailed in AFTA's April 2015 submission global competition for travel services has resulted in margins significantly smaller than those in other parts of the economy such as retail and other services. It is therefore critical that Reform Option G is altered to include the AFTA suggested Framework.

In comment 2 AFTA addresses issues which are of secondary nature yet still impacting on Australian travel agents. AFTA's assessment of these reform options is primarily concerned with lowering the costs to merchants and therefore consumers.

AFTA is supportive of the changes to limit the variations of interchange fees and including Prepaid and international credit cards within the proposed regulation. These changes will reduce ambiguity to business and therefore consumers. AFTA has noted and would welcome additional consultation on companion card changes and potential changes to corporate cards. AFTA requests additional consultation on these issues specifically in regards to implementation of greater transparency measures to allow merchants to identify the different card types.

About Australian travel agents and AFTA

Overview of the Australian Travel Sector

Australian travel agencies currently employ over 35,000 Australians throughout the nation and contributes over \$30 billion annually to the economy across nearly 4000 locations in Australia. Over the past five years the industry has seen significant change but has continued to grow at a rate between 3% - 6% annually. In the 2014/2015 financial year, 83% of all air tickets and 87% of cruise packages were purchased by Australians through either a traditional or online travel agency (IATA, 2015 and CLIA, 2015).

The Australian travel sector contains businesses both large and small, ranging from ASX listed companies, including Flight Centre Travel Group Limited (FLT), Corporate Travel Management (CTD) and helloworld (HLO); to sole operators in small regional towns. Travel agencies are a major employer within the community in which they operate providing sought after professional advice to Australians travelling domestically and overseas both in the leisure and corporate travel space. Importantly for this submission; Australian travel agents conduct 89% of all transactions through electronic means. 40% of these total transactions are conducted using debit / eftpos; 49% are conducted using a credit card; the remainder is conducted with cash (including payments by direct deposit and BPay).

About AFTA

The Australian Federation of Travel Agents Ltd (AFTA) was founded in 1957 to:

- establish professional standards for travel agents;
- stimulate, encourage and promote travel;
- bring together those acting as intermediaries in the distribution of travel-related services;
- build strong working relationships with suppliers and consumers of travel-related services.

As the peak industry body in Australia, AFTA represents the majority of retail travel agents including all of the major travel agency groups. AFTA's membership accounts for approximately 80 percent of Australia's travel intermediaries that control more than 96 percent of travel intermediary turnover. It also has a substantial base of associate members, representing non-intermediary sectors of the travel-related services industry. Members are bound by AFTA's Code of Ethics and are accredited under the national industry scheme known as the AFTA Travel Accreditation Scheme (ATAS).

AFTA represents the interests of its members on many local and international associations and boards, including peak bodies of other national associations. AFTA also contributes significantly to the Australian domestic tourism industry by taking leadership on many challenges and engaging with like-minded industry representative bodies.

AFTA administers Australia's only accreditation scheme for travel agents known as ATAS. ATAS has been endorsed by all state and territory jurisdictions consumer affairs and fair trading departments, following the deregulation of the eight separate legislative regimes governing travel agents from state and territory jurisdiction.

ATAS accredited travel agents are committed to maintaining Australia's world class travel industry. In particular, ATAS accredited travel agents strongly believe in a thriving Australian tourism domestic industry, in which more and more Australians enjoy holidaying at home.

Response to specific issues raised by the RBA

Australian travel agents operate in a highly competitive global market and as such offer competitive electronic payment options for Australian consumers. The recent increase in competition from international domiciled businesses has seen a marked reduction in a travel agent's ability to cover additional costs as a result of domestic regulation. Any additional regulation or changes to the current payment system that the RBA recommends must be viewed from a global perspective, not just a domestic one, ensuring Australian businesses are not disadvantaged. The travel sector is supportive of a number of proposals put forward in the December 2015 Discussion paper with some caveats.

AFTA's primary concern is to ensure that the changes do not increase the business costs specifically, the management FDR and no fault third party chargeback risk. AFTA has sought to address the RBA request for a new approach in reform option G and developed a framework to establish the cost of acceptance in business with FDR and no fault third party chargeback risk. AFTA has also noted that the Draft Standard 3 is noted as the RBA preferred option, AFTA comments have been developed as if this Standard is to be adopted.

Comment 1: Proposed changes to surcharging arrangements - Reform Option G.

The RBA identified that the proposed changes to the surcharging arrangements currently suggested in option 3, does not provide the scope for merchants to include FDR as a cost of acceptance. The RBA noted in the December 2015 Discussion Paper that FDR and subsequent no fault third party charge back is a significant risk for all participants in the payment system and has sought possible solutions to this issue. This issue is only apparent in payments made by credit card and therefore AFTA firmly advocates for its inclusion as cost of acceptance in the final Standard.

For example, consultations have pointed to issues in industries where the 'merchant' is not the ultimate supplier, and the good or service is purchased significantly in advance. Notably, this is the case for travel agents... Given that the cost of chargebacks (or insuring for chargebacks) falls on the merchant, it is not included in the cost of payment services provided by the acquirer.

The cost of chargebacks in this case would not be considered a cost of acceptance under Option 3 and therefore would not be included in the permissible surcharge. The Bank is interested in views on possible alternative approaches – ones that would not excessively complicate the 'cost of acceptance' measure – in cases similar to this (Review of card Payment Regulation Consultation Paper, December 2015, page 32).

As the above extract from the RBA's December 2015 Discussion Paper details, the RBA noted travel agents as an industry segment affected by this issue. Since this issue has been identified by the RBA, ticket providers have also been identified as an affected industry. The common link between travel agents and ticket providers is that they are intermediary between the supplier and consumer. Intermediaries such as travel agents, travel wholesalers and ticketing providers have fostered competition by decreasing the barriers for consumers to find the product or service they desire.

AFTA's 2015 industry survey found that the FDR and therefore subsequent no fault third party chargeback exposure for the Australian travel agent sector is \$5.4 billion for a period of 70-120 days. This is substantially more than 'direct sale' companies, including retail and supermarkets where the FDR would be at a maximum of 30 days. This risk is carried on merchant's books and acquirers view this risk as an unsecured debt which must be mitigated. The management of this risk is a challenge faced by both large and small merchants. This is due to the size of the travel industries FDR. Acquirers regularly review and request bonding arrangements to reduce the impact of no fault third party chargeback on the banks acquiring business.

An intermediary's costs of acceptance are higher than other industries, because FDR is viewed as an unsecured debt by potential acquirers. The cost associated for FDR and no fault third party supplier failure varies dependant on a merchant's transaction value, industry systems and macro-economic events. While rigorous due diligence is conducted by merchants to establish and maintain the credentials of a supplier, intermediaries do not have oversight of all aspects of a supplier's business or economic events. This is one of the principle reasons why acquirers are unable to *price this as a cost of payment services*. It has therefore been the responsibility of the merchants to implement risk management strategies to mitigate this risk at the request of the acquirer. While techniques have varied, larger merchants can demonstrate mitigation strategies using their balance sheet, but smaller merchants are extremely vulnerable to excessive bonds charged by the acquirers. In AFTA's April 2015 Submission it was noted that some travel agents have had requests for bonds of greater than \$1 million to maintain a merchant terminal over the past five years. If a bond is unable to be paid the merchant terminal has been removed limiting the businesses opportunity for growth.

The framework which is detailed in Attachment 1, should be included in the regulation to clearly measure the FDR and no fault third party chargeback risk. The Framework provides a definition of an intermediary and allows the RBA to assess the overall risks, based on agreed variables with specific weightings attached. The framework addresses the variables resulting from a merchant's high level of exposure to FDR and no fault third party chargeback allowing a percentage figure for the applicant to apply to their surcharge by direction of the RBA. To ensure small businesses are not adversely affected by these changes, AFTA submits that group applications for merchants operating below an agreed turnover should be permitted. This will further simplify the surcharge regulations and will also assist in decreasing the compliance costs for small business.

The policy outcomes of this framework will ensure merchants have sufficient liquidity to cover the FDR and continue providing multiple payment options for consumers. For consumers they will now have a comprehensive understanding of the costs associated with their payment choice while maintaining their right to request a chargeback for supplier failure. Importantly the RBA would assess the application and approve an additional element of the surcharge rate. This additional rate could then be applied by the merchant on top of the merchant price on all credit card transactions. The RBA would then forward the approved rates to the ACCC as the enforcement authority allowing the ACCC to conduct compliance reviews. This framework would therefore enforceable by the ACCC as proposed in option 3. AFTA understands the RBA concerns with adding unnecessary complexity to the surcharging arrangements. Nevertheless, the size and nature of this issue for intermediaries requires a solution and AFTA framework seeks to address the RBA's request for a possible transparent solution. AFTA stands ready to discuss this further with all participants in the payment system to evolve the proposed framework in Attachment 1.

Lastly AFTA is concerned that with the removal of the blended surcharge rate, merchants such as travel agents are not able to use blended rates to cover the cost of accepting different 'value' credit cards. AFTA strongly disagrees with the RBA's statement defining *a narrow cost of acceptance will better approximate the incremental cost for many merchants*. While there are costs of acceptance for all payment methods, a consumers' choice to pay using a high cost credit card should not be allocated to the merchant to fund. If the attempt by the RBA is to accurately price signal the cost of acceptance, this statement appears to not be aligned policy objectives of this review. This is further discussed in Comment 2.

Surcharging for intermediaries is a fundamental aspect of a travel agent business model and one that consumers accept. This is because of the omni-channel approach that consumers use, overall margins in the sector are significantly lower than those in 'direct sales' such as retail. In narrowing the cost of acceptance to limit excessive surcharging intermediaries such as travel agents are being asked to cover costs associated with a consumers' choice to use a credit card. AFTA does not believe that Reform Option G, Option 3 adequately addresses the complexities of an intermediaries FDR.

Therefore, further adjustments are needed as suggested in Attachment 1 to ensure FDR is recognised.

Comment 2: Other Reform Options.

As stated in AFTA's April 2015 submission, AFTA believes that there is a need to renew and simplify the current electronic payment system. The simplification of interchange will have downward pressure on costs particularly for small businesses. The ability for merchants to be able to identify the 'type and value of a card' in a card and card-less environment is of critical importance. This is because interchange variances can no longer be mitigated through a blended surcharge rate. This is further explored below within each of the relevant RBA's reform options.

AFTA is also concerned that without adequate industry education many of these reform options will not be successful. This is especially the case for small businesses where it would be appropriate for the RBA to partner with National Associations such as AFTA, to deliver education programs nationally. Education programs run through national associations will ensure sector specific customisation of content and ensure merchants are informed about the changes.

Reform option A - Companion cards

The RBA noted that their preferred choice is option 3. AFTA's members have reported that there has not been a marked increase in usage of American Express Cards. While the change would have limited impact on payment preferences for consumers, the RBA would be creating a two tiered regulatory environment.

This will create greater opportunity for confusion for travel agents on when to apply the relevant surcharge. This change should only be implemented once merchants have the ability to identify which cards will be designated and which are not.

Reform option B – Interchange fees (corporate cards)

As noted in the RBA Discussion Paper, the travel sector does have a higher than average corporate card use. AFTA in-principal supports the inclusion of corporate credits however notes the business model that supports corporate cards is markedly different to non-corporate cards.

AFTA is therefore not opposed to the de-coupling of corporate cards from the interchange as long as merchants are able to surcharge at a higher rate than that of non-corporate cards. Ensuring that businesses have access to corporate cards must not be restricted, nor reduce competition under any proposed reform. AFTA requests the RBA to further consult on this issue.

Reform option C – International cards

AFTA members have reported an increase in usage of international cards specifically within certain travel agent customer segments. There has been an increased volume of air tickets and accommodation bookings within Australia using international cards for use by visiting friends and relatives. This has resulted in increased costs for agencies specialising in this market segment who are typically small businesses.

AFTA supports the RBA's preliminary assessment to support option 2, that international cards should be treated similarly to domestic cards. While this should place downward pressure on the costs for acquirers, AFTA submits monitoring by the RBA is required to ensure these lower costs are provided to the merchant.

Reform option D – Prepaid cards

AFTA supports the RBA's assessment that option 3 include Pre Paid cards within the proposed regulation. This option will remove any ambiguity for prepaid cards for merchants and consumers by including this card type in the new regulation.

As noted in Reform Option A, it is critical that merchants are able to identify the type of card they are accepting.

Conclusion and next steps

Overall AFTA notes the substantial progress made by the RBA in the December 2015 Discussion Paper. However, of particular concern for AFTA is that the RBA and Government, while appreciating the size of FDR and no fault third party chargeback risk faced by travel agents, does not appear to have a possible solution from the regulators. This highlights the current RBA and Government approach to implement a one size fits all approach is not congruent in a modern payment environment. It further emphasises the need for further consultation on surcharging by the RBA and Commonwealth Government with industry segments including intermediaries.

While AFTA appreciates that there has been substantial public concern about surcharging through the Financial System Inquiry, this appears to be directed towards two specific industries. There appears to be little material evidence to indicate that excessive surcharging was an economy wide issue. With this being the case the policy decision to remove blended surcharges appears to be a response to the issues of two industries. The outcome will damage the competitiveness of many small businesses including travel agents who will no longer be able to manage their FDR.

AFTA has developed a possible solution for consultation in regards to management of FDR and no fault third party chargeback. However, it is apparent that the simplest model for managing this risk is through the blended surcharge, which consumers and business alike understand. AFTA again appreciates the RBA facilitating consultation on the possible reform options. AFTA looks forward to further consultation to ensure Australian travel agents are not at a disadvantage as result of any proposed changes.

Attachment 1- Framework to assess Forward Delivery Risk

Objective of the Framework:

To provide the RBA the settings on which to determine the cost to the merchant of the FDR and potential subsequent no fault third party charge back. This will then be used to establish the percentage fee a consumer should pay if they choose to pay via credit card.

This framework will only apply to transactions that are completed using a credit card as defined in the Standard 3, Section 2.3. *(if adopted)*

Definition of eligible intermediaries:

An intermediary is defined as the following;

A company with an Australian Business Number who arranges, take payment for a good or service and the subsequent good or service is delivered or provided by an external supplier.

OR

Travel agents that are members of AFTA and have been assessed to have met standards of AFTA's Travel Accreditation Scheme (ATAS).

Variables for consideration by the regulator:

- The average period the merchant carries the FDR.
- Total current financial exposure and forecasted exposure classified FDR.
- Risk assessment of suppliers and or industry historic trends to establish the possibility of no fault third party charge back.
- Period of time the consumer has the right to lodge a chargeback request.

AFTA proposes that a weighting be given to each of these factors. The weighting of each variable would be established within the regulation to ensure transparency for merchants and consumers.

Provision of FDR acceptance:

In the application the applicant would need to nominate their preferred mitigation strategy. These two options allow small and large business to ensure the most effective mitigation strategy is implemented.

1. FDR and no fault third party chargeback would be managed through the businesses balance sheet with the additional liquidity from a surcharge generated offsetting the FDR on the balance sheet.

OR

2. Merchants attain an insurance policy which would cover the FDR for their business. The premium would then be via a surcharge in each credit card payment.

Assessment of application:

To ensure the process is consistent and efficient the application should be completed with the instruction on the regulator to find fault with the application. The review and finalised decision must be completed within 90 days of lodgement. If no fault is found or the applicant has not been advised of the result, the applicant will consider the application to be approved. Once approved the applicant will proceed with the percentage figure detailed in the application.

Approval period:

On average the length of the FDR is 200 days for the identified merchants. However, contracts for the goods and services to be provided are negotiated on average one to two years prior. To ensure merchants have the stability to plan and ensure sound business decisions, AFTA proposes an approval period of not less than two years, preferably three.

Policy Regulator:

To ensure the ongoing stability of the electronic payment settings, this framework would form part of the Standard for surcharging which is governed by the Payments System Board. The Payment System Board has responsibility under the Reserve Bank Act 1959, to promote efficiency of the payment system while controlling the risk to ensure the stability of the financial system. The RBA is therefore uniquely positioned to have the means to adequately assess the primary and secondary risks within the intermediaries' business models in regards to their FDR.