PROPOSED CHANGES TO THE CREDIT CARD INTERCHANGE STANDARD

A CONSULTATION DOCUMENT – JULY 2005

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Proposed Changes to the Credit Card Interchange Fee Standard

1. Introduction

This Consultation Document proposes a change to the standard on credit card interchange fees. The effect of the change would be to establish a common benchmark interchange fee in the Bankcard, MasterCard and Visa credit card schemes.

The Consultation Document is structured as follows. Section 2 provides some relevant background, including a discussion of the current arrangements for setting interchange fees and the potential for these arrangements to affect competition amongst the credit card schemes. Section 3 summarises the consultation undertaken to date by the Bank on whether a change to current arrangements is warranted. Section 4 discusses the various options considered by the Bank, while Section 5 sets out the proposed modifications to the existing standard. Two alternative standards are proposed for the purposes of consultation. Both would achieve the same objective but would involve different calculation processes for scheme participants. The draft revised standards have been gazetted as required under the *Payment Systems (Regulation) Act 1998*.

Submissions are invited on the draft revised standard by 23 August 2005. As is usual practice, all submissions will be placed on the Bank's website and an opportunity will be provided to those making submissions to discuss them with the Bank. Submissions should be addressed to:

Head of Payments Policy
Reserve Bank of Australia
GPO Box 3947
Sydney NSW 2001
or
pysubmissions@rba.gov.au

2. Background

In April 2001, the Bank designated the Bankcard, MasterCard and Visa credit card schemes as payment systems under the *Payment Systems (Regulation) Act 1998*. It then, in August 2002, determined a standard for interchange fees in each of these schemes.[1]

The standard requires that in each scheme the weighted-average interchange fee be no higher than a benchmark determined on the basis of a set of eligible costs specified in the standard. The eligible costs include issuers' authorisation and processing costs, fraud-related costs, and the cost of funding the interest-free period.

1 *Reserve Bank of Australia* Media Release *2002-15, 27 August 2002.*

The initial benchmarks came into force on 30 October 2003. They are due to be recalculated no later than 30 September 2006, with the revised interchange fees taking effect from 1 November 2006.

The credit card schemes are not required to publish their benchmarks, although each scheme is required to publish all interchange fees set by the scheme. The average interchange fee is lowest in the Bankcard system and highest in the MasterCard system (see Table 1). The differences in interchange fees across the schemes reflect differences in the weighted-average eligible costs of issuers in the schemes.

Table 1: Interchange Fees, June 2005
Per cent of transaction value

	Bankcard	MasterCard	Visa
Standard*	0.49	0.62	0.60
Electronic*	0.49	0.46	0.44

*The electronic rate applies to transactions where the card is swiped and the signature verified. The standard rate applies to most other transactions, including those using manual processing and those over the internet or telephone. MasterCard and Visa also have separate interchange fees for commercial cards.
Sources: Bankcard, MasterCard and Visa websites

Recently, some participants in the credit card schemes have argued that the scheme with the highest interchange fee enjoys a competitive advantage over other schemes. In particular, they have argued that issuers have an incentive to issue cards under the scheme with the highest interchange fee, as the high fee delivers more revenue per dollar spent by cardholders.

Whether this competitive advantage exists or not depends, in part, on whether the additional revenue is offset by additional costs. Here, two types of costs are relevant: those that are scheme specific and those that are issuer specific.

One of the eligible costs included in the standard is the fees charged to issuers by the schemes. To the extent that differences in interchange fees are fully explained by differences in these scheme-specific costs, there would appear to be little incentive to issue cards in the scheme with the highest interchange fee. While issuing cards in this scheme would generate greater interchange revenue, this revenue would be offset by higher payments to the scheme.

There is, however, one qualification to this argument. A scheme with higher scheme fees, and hence a higher cost-based benchmark, may obtain a temporary advantage over other schemes by rebating the scheme fees to its issuers. Issuers would thus receive the higher interchange fee but, after the rebate, would not pay it away in higher scheme fees. While this could provide a competitive advantage to the scheme (in attracting issuers) for a period of time, the benchmark, and thus the interchange fee, would be lowered when the benchmark was recalculated (since the scheme fees net of rebates are used in determining the benchmark).

While scheme-specific costs are potentially important in understanding the competitive dynamics, they account for a relatively small share of total eligible costs. Most of the eligible costs are specific to the issuer – these include the cost of fraud and fraud mitigation as well as the cost of the interest-free period. To the extent that these costs are largely invariant to which scheme cards are issued under, there may be an incentive to issue cards under the scheme with a relatively high interchange fee.

While the Bank has access to the cost data that underlie the calculation of the benchmark, it is not at liberty to disclose the data and thus the precise reasons for the differences in interchange fees. These data, however, indicate that the differences across the schemes are not fully accounted for by differences in scheme fees. Within a scheme there is significant variation in the eligible costs reported by various issuers, partly reflecting variation across issuers in the characteristics of their cardholders. For example, an issuer with a high percentage of cardholders who pay off their balance by the due date is likely to report higher eligible costs than other issuers. If this issuer issues cards predominately in one scheme then that scheme's eligible costs will be higher, and thus so too will the benchmark. Other issuers may then be attracted to this scheme to benefit from the higher interchange fee.

Given the potential for the current arrangements to affect competition amongst the schemes, the Bank called for submissions earlier this year on whether the credit card standard should be varied so that the same cost-based benchmark applied in all the designated credit card schemes.[2]

3. Consultation

In response to its call for submissions, the Bank received nine submissions. While only seven of these were received by the closing date, all submissions were considered, and all are available on the Bank's website. In addition, the Bank provided an opportunity to those who had made submissions to discuss their submissions with the Bank; five parties took up this opportunity.

One group (the majority) argued that the Bank should change the standard to require a common cost-based benchmark for all designated schemes.[3] These parties argued that the current differences in interchange fees, particularly the difference of two basis points in Visa's and MasterCard's fees, is a factor in the marketplace.

Amongst the submissions supporting a common benchmark fee there were two broad approaches advocated.

The Australian Merchant Payments Forum (AMPF) argued that a single benchmark should be established based on the costs of the lowest-cost scheme. Other submissions did not support this approach on the basis that it would result in Bankcard's costs providing the benchmark. They argued that Bankcard's costs reflect those of a small, domestic scheme and are not representative of the costs of credit card issuing more generally. Visa, in particular, argued that Bankcard's costs are not reflective of a growing dynamic network and that if the Bank were to adopt such a benchmark, the capacity of schemes to develop new products for the benefit of society would be reduced.

The second, and more widely supported approach was to base a common benchmark on the weighted-average costs across the schemes. Some submissions argued that Bankcard should

2 *Reserve Bank of Australia* Media Release *2005-02, 24 February 2005.*
3 *See submissions by ANZ, the Australian Merchant Payments Forum, CreditLink, CUSCAL, National Australia Bank and Visa.*

be excluded from this weighted-average on the basis that its costs are not representative of the industry as a whole.

In contrast to the submissions supporting a common benchmark, MasterCard and the Commonwealth Bank argued that the credit card interchange standard should not be changed.

MasterCard argued that instituting a common benchmark would eliminate the remaining competition in the setting of interchange fees. It also argued that competition between issuers with respect to product offerings, and between schemes with respect to scheme fees, would be diminished. MasterCard also argued that a common benchmark would result in under compensation of issuers in the higher-cost scheme and over compensation of those in the lower-cost scheme.

The Commonwealth Bank argued that if a cost-based methodology is to apply, it should reflect actual costs incurred; an outcome which would not be achieved by setting a common benchmark. It also argued that facilitating different interchange fees between schemes is pro-competitive. The Commonwealth Bank also noted that, in its view, the independent experts appointed by the Schemes to calculate their benchmarks, play an important role and it would be undesirable to abolish this role.

Westpac indicated that it was not convinced of the need for change but, if the Bank were to institute such a change, it would support a common benchmark determined by costs averaged across the three schemes.

The issue of timing was also addressed in consultation. There was general agreement that, should a change be made, it should be implemented at the same time as the benchmarks are recalculated in 2006. There was also a view that any change should be announced as soon as possible so that participants could take it into account in their planning.

4. Options

In response to the consultation, the Bank has considered two broad options. The first is to leave the current credit card interchange standard unchanged and the second is to revise the standard to set a common cost-based benchmark for all the designated credit card schemes.

The consultation process confirmed that the current arrangements have created, at the margin, an incentive for issuers to issue credit cards under the scheme with the highest interchange fee. This is despite the difference in interchange fees in the two largest schemes being only two basis points.

A number of issuers noted that cardholders have shown themselves to be quite accepting of changes in the brand of credit card. This means that the cost to issuers of encouraging customers to move from one scheme to another may be minimal in terms of customer loss and, if the scheme pays for reissuing cards, minimal in total. The potential for significant shifts between schemes in these circumstances is therefore quite high because not only new issuers, but also existing issuers, could be encouraged to issue cards under the scheme with the higher interchange fee.

The consultation process also highlighted the fact that there is little competitive discipline on schemes with relatively high interchange fees. While higher interchange fees mean higher costs to acquirers, these higher costs are not transparently passed on to merchants who are invariably offered a bundled price for accepting all three designated credit card schemes. As a result, a scheme with relatively high fees does not find itself at a competitive disadvantage in terms of merchant acceptance. This would likely remain the case even if acquirers charged merchants more for accepting the higher-cost scheme given that merchants have demonstrated that they find it difficult to reject higher-cost cards.

Some submissions argued that the recalculation of the current benchmarks every three years will ameliorate any competitive advantage enjoyed by the scheme with the highest interchange fee. In particular, as lower-cost issuers are attracted to the scheme with the high interchange fee, the benchmark will fall when it is recalculated, offsetting the gain those issuers achieved from switching. However, the offset would not be complete and, thus, an incentive to switch to the scheme with the relatively high benchmark would remain. Even if the offset were complete, some issuers claimed that a year or two of higher interchange fees is of commercial benefit and worth the costs of a switch in brands.

In comparison with the current arrangements, a common interchange fee would provide a stronger incentive towards cost savings (that is technical efficiency) and promote more soundly based competition between the schemes for issuers.

A common benchmark would mean that lower-cost schemes could use their lower costs to attract issuers. Under current arrangements, issuers are not very sensitive to the scheme costs included in eligible costs: if scheme costs are low the interchange fee is low and if scheme costs are high the interchange fee is high. In contrast, under a common benchmark fee, issuers are likely to find it more attractive to issue cards under schemes with the relatively low scheme costs. The result should be a more efficient system.

This analysis also argues for a benchmark based on an average of scheme costs rather than one based on the lowest-cost scheme. If the benchmark is based on the costs of the lowest-cost scheme, there is little incentive for that scheme to lower its costs further as it will lose the benefit of the cost savings when the benchmark is recalculated. If instead the benchmark is based on costs averaged across the schemes, the low-cost scheme will retain a portion of its cost savings even after the benchmark is recalculated – thus providing a stronger incentive to lower costs.

These arguments contrast with those put by MasterCard which emphasised a detrimental effect on competition of a common benchmark.

MasterCard argued that a common benchmark would ‘eliminate to a great extent the remaining degree of competition between the credit card schemes in the setting of interchange fees’ and that the schemes should be allowed to set interchange fees themselves. In contrast, the Bank's view is that interchange fees are not set under normal competitive conditions, with competitive pressures tending to push interchange fees up not down.

MasterCard also argued that a common benchmark would lead to greater homogeneity in credit card offerings in the Australian market place and increase the attractiveness of the three-party schemes to issuers. The Bank does not accept either of these arguments. There is strong competition amongst issuers of credit cards in terms of both price and product characteristics. In the Bank's opinion, this situation would not be adversely affected by a common benchmark interchange fee. Similarly, a common benchmark fee, at around the current level of interchange fees, is unlikely to increase the attractiveness of the three-party schemes to issuers, since it would not change the average interchange revenue of issuers in the four-party schemes.

Finally, MasterCard argued that a common benchmark would 'under-compensate the issuers in the more expensive scheme(s), and over-compensate the issuers in the lower-costing scheme(s)'. As noted above, the Bank's opinion is that a common benchmark would improve the incentives for the schemes to lower their costs and for issuers to issue under the lower-cost scheme. Also, it is worth noting that under current arrangements the eligible costs of issuers span quite a wide range, with some issuers having lower costs than the relevant benchmark, and others having higher costs than the benchmark.

Taking into account the submissions and consultations and its own analysis, the Payments System Board has reached the preliminary conclusion that the establishment of a common benchmark would be in the public interest.

5. A Draft Revised Standard

In deciding on the specific variations to the existing standard, the Bank considered a number of issues. These included: how a common benchmark should be established; the date on which a revised standard would come into effect; and the mechanics of the calculation. On the first two issues, the Bank has clear preferences, which are explained below. On the third, it can see two viable options for calculation which arrive at essentially the same result. To give interested parties the opportunity to comment, the Bank has released two draft Standards that incorporate these alternative methods of calculation, only one of which would be adopted.

In general the revised standards use the same language as the existing credit card interchange standard, except where revisions are necessary to give effect to the changes discussed above. There are, however, two minor further variations. The first deals with the selection of nominated scheme participants (in version A) and nominated participants (in version B). The second relieves participants in the schemes from the obligation to certify compliance with the Standard; the administrators of the schemes remain responsible for doing so.

A common benchmark

The Bank considered two ways in which a common benchmark could be determined. The first is to use the weighted-average eligible costs of the designated credit card schemes and the second is to use the eligible costs of the lowest-cost scheme.

The former option is the Bank's preferred approach. This reflects two considerations. The first is that this option will, as discussed above, promote stronger incentives for all schemes to lower their costs. The second is that using the lowest-cost scheme would lead to a significant drop in the average level of interchange fees in the Australian credit card industry. This is not the Bank's intention; the proposed change is aimed at improving incentives, rather than reducing the overall level of interchange fees. At this stage, the Bank's view is that it would be inappropriate to lower average fees without more extensive analysis and consultation. The Bank has previously noted that it will conduct a review of arrangements in 2007.

A related matter is the treatment of Bankcard in any such weighted-average benchmark. Some submissions argued for the exclusion of Bankcard on the grounds that it is considerably different from the other schemes (predominantly because it is a domestic scheme rather than an international scheme). The Bank's view, however, is that there is a stronger case to include all the designated schemes. Both draft standards therefore propose that Bankcard be included in a weighted-average benchmark.

Timing of the change

A common view in consultations was that any change to the method of calculating a common benchmark should be made at the same time as the scheduled 2006 recalculation of the benchmarks. The Bank supports this view and both draft standards propose a commencement date of 1 July 2006.

The mechanics of the calculation

The Bank considered two approaches to calculating the weighted-average benchmark, both of which yield essentially the same result.

In the first, which is set out in Version A, each scheme would continue to appoint an independent expert to calculate a cost-based benchmark. These benchmarks would be provided to the Bank along with the value of transactions on which they are based. The Bank would then weight the cost-based benchmarks by relative transaction values in each scheme to calculate the common cost-based benchmark to apply to all three schemes. Under this approach, the current processes would remain in place but one more step would be added – that of the Reserve Bank calculating a weighted-average common benchmark. Issuers would still be required to allocate costs between schemes, with a different set of issuers potentially being included in the calculations for each scheme. Each scheme would propose an independent expert, who would be agreed to by the Reserve Bank.

In the second approach, which is set out in Version B, the scheme-based calculations would be abandoned. Instead, the Bank would nominate those issuers that account for at least 90 per cent of the value of credit card transactions in the designated schemes. An independent expert proposed by the issuers in the schemes, and agreed to by the Reserve Bank, would then be provided with eligible costs by each of the nominated issuers. These costs would be added together and divided by the total value of credit card transactions undertaken on credit cards issued by the nominated issuers, to yield a common cost-based benchmark. The key difference between this approach and the first one is that there would be no need for each issuer to allocate costs between schemes – eligible costs would be those relating to credit card issuing in total. In addition, members of the schemes would only need to meet the cost of one independent expert rather than three experts.

Standard No. (..) A

The Setting of Wholesale ('Interchange') Fees in designated credit card schemes

Objective

The objective of this Standard is to ensure that the setting of wholesale ('interchange') fees in the designated credit card schemes is transparent and promotes:

(i) efficiency; and

(ii) competition

in the Australian payments system.

Application

1. This Standard is determined under Section 18 of the *Payment Systems (Regulation) Act 1998*.
2. This Standard applies to the payment systems operated within Australia known as the Bankcard scheme, the MasterCard system and the Visa system, each of which was designated as a payment system on 12 April 2001 by the Reserve Bank of Australia under Section 11 of the *Payment Systems (Regulation) Act 1998*, and referred to as follows as 'the Schemes'.
3. In this Standard:

   an 'acquirer' is a participant in any of the Schemes that provides services to a merchant to allow that merchant to accept a credit card;

   'credit card' means a card issued under the rules of any of the Schemes that can be used for purchasing goods or services on credit, or any other article issued under the rules of any of the Schemes and commonly known as a credit card;

   'credit card transaction' or 'transaction' means a transaction in Australia between a credit cardholder and a merchant involving the purchase of goods or services using a credit card;

   'financial year' is the 12-month period ending 30 June;

   an 'issuer' is a participant in any of the Schemes in Australia that issues credit cards to the issuer's customers;

   'merchant' means a merchant in Australia that accepts a credit card for payment for goods or services;

   'nominated Scheme participants' for each Scheme are those issuers in each Scheme that, when selected in order of their share of the value of credit card transactions in the Scheme in Australia in the financial year prior to the date by which the applicable cost-based benchmark must be calculated, are the minimum number of issuers to account for at least 90 per cent of those transactions, those issuers being determined by the administrator of the Scheme or the other participants in the Scheme in Australia;

'rules of the Scheme' mean 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 consider themselves bound;

terms defined in the *Payment Systems (Regulation) Act 1998* have the same meaning in this Standard.

4. This Standard refers to wholesale fees, known as 'interchange' fees, which are payable by an acquirer, directly or indirectly, to an issuer in relation to a credit card transaction in any of the Schemes.

5. Each participant in any of the Schemes must do all things necessary on its part to ensure compliance with this Standard.

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

7. This Standard is to be interpreted:
   - in accordance with its objective; and
   - by looking beyond form to substance.

8. This Standard comes into force on 1 July 2006 and the benchmark set under it will become effective from 1 November 2006.

9. This Standard will replace Standard No. 1, *The Setting of Wholesale ('Interchange') Fees* which applies to each of the Schemes individually. The benchmark determined under that Standard will be effective until 30 October 2006.

Interchange fees

10. On each of the dates specified in paragraph 11, the average of interchange fees implemented in each of the Schemes in Australia, calculated in accordance with paragraph 17 below, must not exceed the common cost-based benchmark calculated in accordance with paragraphs 12 to 16 below.

11. For the purposes of paragraph 10, the dates are:
    (i) 1 November in the year in which the relevant common cost-based benchmark is published by the Reserve Bank of Australia; and
    (ii) the date any interchange fee is introduced, varied, or removed.

Methodology

12. The cost-based benchmark for each Scheme is calculated as the total value of eligible costs of the nominated Scheme participants in that Scheme for the financial year

prior to the date by which the cost-based benchmark must be calculated, divided by the aggregate value of credit card transactions for the same period undertaken using credit cards issued by those nominated Scheme participants, and expressed as a percentage. Eligible costs are:

(i) issuers' costs incurred principally in processing credit card transactions, including the costs of receiving, verifying, reconciling and settling such transactions;

(ii) issuers' costs incurred principally in respect of fraud and fraud prevention in connection with credit card transactions;

(iii) issuers' costs incurred principally in providing authorisation of credit card transactions; and

(iv) issuers' costs incurred in funding the interest-free period on credit card transactions, calculated using the average of the cash rate published by the Reserve Bank of Australia over the three financial years prior to the date by which the cost-based benchmark must be calculated.

13. Data on eligible costs must be drawn from accounting records of the nominated Scheme participants, prepared in accordance with generally accepted accounting principles and Australian accounting standards.

14. Data on eligible costs and the total value of transactions of each nominated Scheme participant in each Scheme must be provided by that participant to an independent expert proposed by that Scheme and agreed to by the Reserve Bank of Australia. The expert must review the data to determine if the costs included are eligible costs and must use the data on eligible costs to calculate the cost-based benchmark for that Scheme.

15. The administrator of each Scheme and the nominated Scheme participants for that Scheme must provide to the Reserve Bank by 15 September of the relevant year:

(i) the cost-based benchmark and the data on eligible costs and the value of transactions undertaken by each of the nominated Scheme participants used by the independent expert to calculate the cost-based benchmark;

(ii) the value of transactions undertaken by all of the participants in the Scheme in the previous financial year.

16. The common cost-based benchmark is calculated by the Reserve Bank using as weights the shares of each Scheme in the total value of credit card transactions undertaken in all the Schemes. The Reserve Bank of Australia will publish the common cost-based benchmark by 30 September of the relevant year.

17. The cost-based benchmark for each Scheme must be calculated and provided to the Reserve Bank of Australia by 15 September 2006 and each third anniversary thereafter. If the Reserve Bank of Australia agrees in writing, a recalculation of the cost-based benchmark for each Scheme and of the common cost-based benchmark may be undertaken at other times if changes in eligible costs or other factors warrant.

18. For purposes of paragraph 10, the average of interchange fees in each Scheme is a weighted average calculated as follows:

    (i) each interchange fee rate, net of applicable taxes, is expressed as a percentage of transaction value for the transactions in the relevant Scheme to which that interchange fee rate applies for the financial year prior to the applicable date specified in paragraph 10;

    (ii) the weights to be applied to these percentages are the shares of transactions in the relevant Scheme to which each such interchange fee rate applies in the total value of transactions in the Scheme in Australia for the financial year prior to the applicable date specified in paragraph 10.

Transparency

19. The administrator of each Scheme or a representative of the participants in the Scheme in Australia must publish the interchange fee rates of the Scheme in Australia on the Scheme's website or make the interchange fee rates generally available through other means.

20. The administrator of each Scheme must certify annually in writing to the Reserve Bank of Australia, on or before 30 November each year, that interchange fees of the Scheme in Australia over the prior twelve months ending 31 October were in compliance with this Standard.

Standard No. (..) B

The Setting of Wholesale ('Interchange') Fees in designated credit card schemes

Objective

The objective of this Standard is to ensure that the setting of wholesale ('interchange') fees in the designated credit card schemes is transparent and promotes:

(i) efficiency; and

(ii) competition

in the Australian payments system.

Application

1. This Standard is determined under Section 18 of the *Payment Systems (Regulation) Act 1998*.
2. This Standard applies to the payment systems operated within Australia known as the Bankcard Scheme, the MasterCard system and Visa system, each of which was designated as a payment system on 12 April 2001 by the Reserve Bank of Australia under Section 11 of the *Payment Systems (Regulation) Act 1998*, and referred to as follows as 'the Schemes'.
3. In this Standard:

   an 'acquirer' is a participant in any of the Schemes that provides services to a merchant to allow that merchant to accept a credit card;

   'credit card' means a card issued under the rules of any of the Schemes that can be used for purchasing goods or services on credit, or any other article issued under the rules of any of the Schemes and commonly known as a credit card;

   'credit card transaction' or 'transaction' means a transaction in Australia between a credit cardholder and a merchant involving the purchase of goods or services using a credit card;

   'financial year' is the 12-month period ending 30 June;

   an 'issuer' is a participant in any of the Schemes in Australia that issues credit cards to the issuer's customers;

   'merchant' means a merchant in Australia that accepts a credit card for payment for goods or services;

'nominated participants' are those issuers that, when selected in order of their share of the value of credit card transactions of all the Schemes in Australia as reported to the Reserve Bank of Australia in the financial year prior to the date by which the applicable cost-based benchmark must be calculated, are the minimum number of issuers to account for at least 90 per cent of those transactions, those issuers being determined by the Reserve Bank of Australia;

'rules of the Scheme' mean 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 consider themselves bound;

terms defined in the *Payment Systems (Regulation) Act 1998* have the same meaning in this Standard.

4. This Standard refers to wholesale fees, known as 'interchange' fees, which are payable by an acquirer, directly or indirectly, to an issuer in relation to a credit card transaction in any of the Schemes.
5. Each participant in any of the Schemes must do all things necessary on its part to ensure compliance with this Standard.
6. If any part of this Standard is invalid, it is ineffective only to the extent of such part without invalidating the remaining parts of this Standard.
7. This Standard is to be interpreted:
   - in accordance with its objective; and
   - by looking beyond form to substance.
8. This Standard comes into force on 1 July 2006 and the benchmark set under it will become effective from 1 November 2006.
9. This Standard will replace Standard No. 1, *The Setting of Wholesale ('Interchange') Fees* which applies to each of the Schemes individually. The benchmarks determined under that Standard will be effective until 30 October 2006.

Interchange fees

10. On each of the dates specified in paragraph 11, the average of interchange fees implemented in each of the Schemes in Australia, calculated in accordance with paragraph 17 below, must not exceed the common cost-based benchmark calculated in accordance with paragraphs 12 to 16 below.
11. For the purposes of paragraph 10, the dates are:
    (i) 1 November in the year in which the relevant common cost-based benchmark is published by the Reserve Bank of Australia; and
    (ii) the date any interchange fee is introduced, varied, or removed.

Methodology

12. The common cost-based benchmark is calculated as the total of eligible costs for the nominated participants for the financial year prior to the date by which the common cost-based benchmark must be calculated, divided by the total value of credit card transactions for the same period undertaken using credit cards of all the Schemes issued by the nominated participants, and expressed as a percentage. Eligible costs are:

    (i) issuers' costs incurred principally in processing credit card transactions, including the costs of receiving, verifying, reconciling and settling such transactions;

    (ii) issuers' costs incurred principally in respect of fraud and fraud prevention in connection with credit card transactions;

    (iii) issuers' costs incurred principally in providing authorisation of credit card transactions; and

    (vi) issuers' costs incurred in funding the interest-free period on credit card transactions, calculated using the average of the cash rate published by the Reserve Bank of Australia over the three financial years prior to the date by which the cost-based benchmark must be calculated.

13. Data on eligible costs must be drawn from accounting records of the nominated participants, prepared in accordance with generally accepted accounting principles and Australian accounting standards.

14. Data on eligible costs and the total value of transactions of each nominated participant must be provided by that participant to an independent expert proposed by the nominated participants and agreed to by the Reserve Bank of Australia. The expert must review the data to determine if the costs included are eligible costs.

15. The independent expert and the nominated participants must provide the data on eligible costs of each nominated participant and the total value of transactions of each of the nominated participants to the Reserve Bank of Australia by 15 September of the relevant year. The Reserve Bank of Australia will calculate the common cost-based benchmark by 30 September and publish it on its website.

16. The common cost-based benchmark will be calculated by 15 September 2006 and by each third anniversary thereafter. If the Reserve Bank of Australia agrees in writing, a recalculation of the common cost-based benchmark may be undertaken at another date if changes in eligible costs or other factors warrant.

17. For purposes of paragraph 10, the average of interchange fees in each Scheme is a weighted average calculated as follows:

    - each interchange fee rate, net of applicable taxes, is expressed as a percentage of transaction value for the transactions in the relevant Scheme to which that interchange fee rate applies for the financial year prior to the applicable date specified in paragraph 10;

- the weights to be applied to these percentages are the shares of transactions in the relevant Scheme to which each such interchange fee rate applies in the total value of transactions in the Scheme in Australia for the financial year prior to the applicable date specified in paragraph 10.

Transparency

18. The administrator of each Scheme or a representative of the participants in the Scheme in Australia must publish the interchange fee rates of the Scheme in Australia on the Scheme's website or make the interchange fee rates generally available through other means.
19. The administrator of each Scheme must certify annually in writing to the Reserve Bank of Australia, on or before 30 November each year, that interchange fees of the Scheme in Australia over the prior twelve months ending 31 October were in compliance with this Standard.