



Mr Rod Sims
Chair
Australian Competition and Consumer Commission
23 Marcus Clarke Street
Canberra ACT 2601
Via email: forex@accc.gov.au

29 October 2018

Dear Mr Sims,

Inquiry into Foreign Currency Conversion Services

Thank you for the opportunity to provide a submission to the Inquiry into Foreign Currency Conversion Services.

We are pleased to provide you with this submission clarifying Mastercard's role in foreign currency conversion services. The services we provide in transaction processing, foreign currency conversion and other services are to card issuers and acquirers, and not directly to consumers and small business.

Card payments for cross-border transactions provide enormous value to consumers and businesses. As noted by the ACCC in the issues paper, card payments can increase competitive pressure in foreign currency exchange services. This was also highlighted in research commissioned by Mastercard across ten markets, which is outlined below.

In addition to responding to your Issues Paper, we also draw your attention to the issue of Dynamic Currency Conversion, a matter the Commission may wish to examine in more detail.

If you require further information or would like to discuss any aspect of this submission further, please contact [REDACTED], Director Public Policy [REDACTED] [REDACTED] or via email to [REDACTED]

Yours sincerely

[REDACTED]

[REDACTED]

Division President Australasia

About Mastercard

Mastercard is a technology company in the global payments industry that connects consumers, financial institutions, merchants, governments, digital partners, businesses and other organisations worldwide, enabling them to use electronic forms of payment instead of cash and cheques.

Through our global payments processing network, we facilitate the switching (authorisation, clearing and settlement) of payment transactions and deliver related products and services.

A typical transaction on our core network involves four participants in addition to us:

- account/card holder (a consumer who holds a card or uses another device enabled for payment),
- merchant,
- issuer (the account holder's financial institution), and
- acquirer (the merchant's financial institution).

Mastercard does not have direct contractual relationships with cardholders or merchants. Such relationships belong to, and are managed by, issuing and acquiring financial institutions. We do not issue cards, extend credit, determine or receive revenue from interest rates or other fees charged to account holders by issuers, or establish the rates charged by acquirers in connection with merchants' acceptance of our branded products.

Mastercard's role in foreign transactions

Mastercard's relationship is with issuing banks and financial institutions who supply those services to their customers. Our role in foreign transaction services in Australia is two-fold:

1. Mastercard's allows consumers and small businesses to transact using their Mastercard product with overseas merchants, both in person and online, as well as allows overseas consumers and businesses to transact with Australian merchants. Cross-border transaction processing over the Mastercard network may involve Mastercard playing a role in relation to currency conversion.
2. Mastercard also operates a business, Mastercard Prepaid Management Services, which provides services to certain institutions that issue prepaid foreign currency cards. Mastercard provides the product platform, processing, back office services and cardholder servicing. In some circumstances, as part of program management services, Mastercard Prepaid Management Services will set the exchange rate on behalf of the issuer.

Mastercard does not charge any fees directly to either cardholders or merchants.

1. Cross-border transaction processing services

Mastercard is part of the supply chain of foreign currency conversion services, providing the network architecture that allows banks and other institutions to issue prepaid foreign currency cards and provide credit and/or debit transaction services to its customers outside the jurisdiction of issuance.

Settlement Services

A financial institution has the option to pick the currency in which they settle their cross-border transactions with Mastercard from a wide range of liquid global currencies. The Australian Dollar ("AUD") is among the currencies offered, allowing Australian banks to settle obligations in their local currency.

Mastercard Issued Currency Conversion Rates

On a daily basis, Mastercard issues currency conversion rates to be used on our network (Mastercard Issued Rates).

The Mastercard Issued Rates are used to calculate:

- (1) The AUD value of each processed transaction made in a non-AUD currency using an Australian Dollar issued Mastercard branded product. These values are communicated by us to issuers (Processed Transaction Amounts).
- (2) The amounts that issuers and acquirers must settle with Mastercard for processed cross-border transactions (Settlement Amounts).

Settlement Amounts

The Mastercard Issued Rates are utilised to determine the amounts issuers need to settle through the Mastercard system for all cross-border transactions performed by their cardholders that are denominated in a currency different from the issuer settlement currency.

For example, if a cardholder travels to the United Kingdom and makes a purchase in British Pounds (GBP), the Mastercard Issued GBP/AUD rate will be used to determine the Australian Dollar amount that the issuer must settle with Mastercard for the transaction.

Processed Transaction Amounts

In addition to a settlement amount, for every processed transaction, Mastercard provides a calculated Processed Transaction Amount that issuers can use in determining the amount they will bill the cardholder for the transaction. Mastercard uses the same Mastercard Issued Rates to calculate such Processed Transaction Amounts as are used to calculate the Settlement Amounts.

In the example above, Mastercard will use the Mastercard Issued GBP/AUD Rate to calculate a Processed Transaction Amount and will provide it to the issuer. Issuers may or may not use the Processed Transaction Amount calculated by Mastercard in their relationship and billing practices with cardholders. Issuers may also add fees or mark-ups to the Mastercard Issued Rates. Mastercard does not have visibility in these matters as the account holder relationships belong to, and are managed by, the issuers.

Mastercard Issued Rates Sourcing

The Mastercard Issued Rates are generally wholesale (interbank) market rates as observed in multiple market sources (e.g. Reuters, Bloomberg), or government mandated rates (e.g., Central Bank rates) where required.

The Mastercard Issued Rates are valid for a 24-hour period: any transaction submitted for processing during the corresponding 24-hour period will be processed using the Mastercard Issued Rates published at the time.

Charges and costs in respect of cross-border transaction processing services

The ACCC has asked for input on the costs to suppliers of foreign exchange services. In this vein, we wanted to provide information on what Mastercard charges its customers for cross-border transaction processing.

We note that Mastercard charges vary depending on the nature and volume of the transactions and the product on which the payment is made but may accurately be summarised as follows.

Cross-border volume fees

Cross-border volume fees are charged by Mastercard to issuers and acquirers based on the dollar volume of activity on cards and other payments devices carrying our brands where the merchant country and the issuer country are different. Typically, a cross-border transaction generates higher charges than a domestic transaction.

Transaction processing fees

Mastercard transaction processing fees apply for both domestic and cross-border transactions and are primarily based on the number of transactions. Transaction processing includes Authorisation, Clearing and Settlement.

Other costs

We observe that other costs exist in cross-border transaction processing. In particular, interchange is a fee paid by a merchant's bank (the acquirer) to a cardholder's bank (the issuer) to compensate the issuer for the value and benefits merchants receive when they accept electronic payments.

Cross-border interchange fees reimburse issuers for costs incurred. Mastercard sets "default interchange fees" that apply when there are no other established settlement terms in place between an issuer and an acquirer. We administer the collection and remittance of interchange fees through the settlement process.

While Mastercard sets default interchange fees, it does not earn revenue from these fees.

Communication of costs

Under Mastercard's Rules (attached) issuers are responsible for transparently communicating cost for using cards for cross-border transactions to their cardholders. We also require merchants to communicate relevant costs, like surcharging or the charging of Dynamic Currency Conversion fees to their customers when they use their card.

In addition, Mastercard provides complete transparency on the rate offered to issuers through our web page <https://www.mastercard.com/global/currencyconversion/>. The web page is available to anyone with an internet connection and in multiple languages in addition to English.

The nature and extent of competition in the Market

As the Issues Paper notes, the market for foreign currency services is highly competitive, characterised by a range of providers and options to obtain foreign currency or make payments in foreign currency. There are now many more options to convert money and pay than cash and travellers' cheques.

Recent technological advances have introduced more choice in the market. Technology has also driven increases in competitive pricing – and in some instances removed the need for a formal currency exchange to occur.

In 2015, Mastercard commissioned benchmarking of foreign currency rates across ten Asia-Pacific markets – Australia, China, India, Indonesia, Japan, Malaysia, New Zealand, Philippines, Singapore and South Korea. The costs of converting currency at exchange bureaus and hotels were compared with the costs of withdrawing foreign currency at ATMs and making foreign debit card purchases¹.

Key findings of this study included:

- Using debit cards instead of cash results in the best currency exchange rates.
- Across the ten markets, ATM Withdrawal and Debit Purchase offer far better value than Airport Exchange Bureaus and Hotels that convert currency. By withdrawing from an ATM or making a direct debit card purchase, travellers saved an average of up to 2.5 per cent compared to hotel exchange rates,

¹ Exchange rates were obtained by confirming rates at exchange bureaus and hotels, withdrawing currency from ATMs using debit cards issued in the home country, and making purchases with debit cards from the home country. For each exchange source, money was exchanged, withdrawn, or used for purchases at two different transaction amounts, a low and high value, from at least two different sources per category.

The implicit, all-in exchange rate was determined for the two different values at each source by dividing FX withdrawn by total cost of the transaction in home currency. Then, the fixed and variable components of the exchange rate at each source were calculated using a straight-line method. The fixed and variable components were then used to determine the net exchange rate at different currency amounts. That exchange rate was then compared to the market exchange rate to determine mark-up. To achieve consistent comparisons across all currency conversion options and corridors, a currency equivalent value of USD300 was used as the exchange denomination for mark-up and savings calculations.

and an average of 4.1 per cent to 6.1 per cent compared to airport exchange bureaus.

- Total savings equated to between USD12.14 and USD18.44 on a USD300 equivalent conversion by using a debit card instead of an airport exchange bureau.

Figure 2. Average mark-up across currency exchange services (Source: Kaiser Associates)

Rank	Exchange Location	Average Markup Over Market
1	Debit Purchase	3.7%
2	ATM Withdrawal	4.2%
3	Hotel Exchange	6.2%
4	Destination Airport Bureau	8.3%
5	Home Airport Bureau	9.8%

It is important to note that the average mark-ups of debit purchases and ATM withdrawals presented above include the impact of bank fees levied by issuers in addition to the impact of the Mastercard Issued Rates which are generally wholesale (interbank) market rates. Also, the mark-ups are not adjusted down for any additional services issuers may be providing to cardholders over the other currency conversion providers (E.g. loyalty points, cash back). As illustrated by the benchmarking study, we believe the effective foreign exchange rates applied to consumer card transactions (whether through point of sale purchases or ATM withdrawals) are highly competitive as compared to other options available to retail consumers.

Mastercard Prepaid Management Services

We note that a number of Australian travellers wish to make transactions overseas with a sense of security coming from an exchange rate known and fixed in advance and wish to purchase pre-paid cards allowing transactions to be made on this basis.

Mastercard Prepaid Management Services (MPMS) is a service provider to institutions that issue prepaid foreign currency cards. These cards can be loaded with funds to the requisite value in foreign currency of the consumer's choice and can be transferred into other non-Australian currencies. Mastercard provides the product platform, processing, back office services and cardholder servicing for such prepaid programs.

The prepaid card issuers set exchange rates for loading the prepaid cards or converting the currency for funds on the card. In some circumstances, as part of program management services, MPMS will set the exchange rate on behalf of the issuer. The exchange rate set by MPMS will be applied by the issuing institution when a cardholder loads funds to a card or transfers funds between currencies. The way MPMS sets rates in such situations is based on a wholesale market rate observed throughout a period immediately preceding the setting of rates plus a currency conversion margin pre-agreed with the issuing institution. MPMS and the issuing institution may share the margin with a part accruing to the issuer and the rest to MPMS.

All exchange rates and fees are communicated clearly to consumers on the product website. Fees are also outlined in the Product Disclosure Statement provided to the cardholder when the card is issued. Customers are able to use this information to make an assessment of the currency conversion rate, as well as associated fees, before they load their card.

Examining Dynamic Currency Conversion (DCC)

Dynamic Currency Conversion (DCC) is a service offered by merchants (generally facilitated through their acquirer or a third-party service provider) that allows cardholders to choose to pay in the cardholder's home currency at the point of interaction with that merchant.

Mastercard believes Dynamic Currency Conversion should be included in the inquiry by the ACCC in the interests of ensuring transparency, protecting and educating consumers about the costs involved, to help them make more informed choices.

International consumer organisations have raised concern about the cost and transparency of DCC. European consumer advocacy group BEUC² reported DCC transactions at ATMs in non-Euro EU countries were between 2.6 per cent and 12 per cent more costly than if they'd been made in local currencies.

There is likely to be significant information asymmetries at the time of payment between consumers and merchants or ATM owners offering DCC. At a hotel, restaurant or car rental agency, cardholders are faced with an immediate, one-off decision to pay in their home or the local currency (which we note is different from multi-currency pricing in e.g. on-line sales). While DCC is positioned as a matter of cardholder convenience, related fees are rarely transparent to the cardholder. Hence we urge the ACCC to consider DCC fee transparency in within the purview of the inquiry including what practically can be done from an Australian perspective to improve the experience of customer choice for Australian cardholders.

² BEUC 30/10/2017 https://www.beuc.eu/publications/beuc-x-2017-118_dynamic_currency_conversion_position_paper.pdf

Conclusion

There are now more ways to make cross-border payments safely and conveniently, than ever before.

Card payments for cross-border transactions provide enormous value to consumers and businesses. As noted by the ACCC in the issues paper, card payments can increase competitive pressure in foreign currency exchange services. Results from several cited studies are in line with this position.

Mastercard believes consumers should always have the final choice on how they pay – whether the transaction is at home or overseas. Consumers need to be armed with appropriate information so they can make this choice.

Beyond the four issues the Commission has sought comment on, Mastercard recommends the ACCC examine DCC in more depth, especially limited of information consumers have at the time they make a DCC transaction.