

29 February 2012

CCAAC Gift Card Review
c/- The Manager
Consumer Policy Framework Unit
Infrastructure, Competition and Consumer Division
Treasury
Langton Crescent
PARKES ACT 2600

Dear Mr Neave,

Heritage Bank appreciates the opportunity to contribute to your inquiry into gift cards in Australia, particularly given our position in the prepaid card market. Heritage is the biggest issuer of Visa prepaid cards in Australia with over 200 separate prepaid card programs and more than 50% market share. We also issue MasterCard prepaid cards, specifically Travelex's multi-currency travel cards (now Access Prepaid International).

While the CCAAC review appears to be directed towards consumer concerns associated with merchant gift cards, the definition of what constitutes a gift card contained in your December 2011 Issues Paper is wider, unambiguously capturing all prepaid cards. On the other hand, the issues identified by the Paper relate almost exclusively to closed loop store gift cards rather than to scheme cards of the type issued by Heritage Bank.

Scheme cards already have robust and stringent consumer protection and product disclosure regulation and oversight in place, from most of which merchant gift cards are specifically carved out. Unlike gift cards, the liability for scheme card balances sits with the issuing ADI, not a merchant, with the financial stability of the ADI overseen by APRA under the Banking Act 1959. Being open loop, scheme cards can be used at most merchants (including online) and card balances can normally be supplemented with cash to complete transactions. Cash can typically be withdrawn at ATMs.

The reason for this submission is therefore simple.

Heritage wishes to ensure that CCAAC recommendations meant to address issues specific to closed loop merchant gift cards do not inadvertently also capture highly regulated scheme based cards where consumers are already strongly protected.

Yours sincerely,



Peter Cavanagh
General Manager Strategy

INTRODUCTION

Heritage Bank is a leading issuer of open loop prepaid cards in the Australian market, issuing cards that operate using both the Visa and MasterCard schemes on behalf of over 200 programs. While the consumer concerns highlighted and discussed in the December Issues Paper appear to relate specifically to closed loop merchant gift cards, Heritage is concerned that the definition in the Paper of what constitutes a gift card includes open loop cards that are quite different products.

Heritage therefore requests that open loop scheme based cards be specifically excluded from any recommendations made by the Committee to address the consumer issues identified in the Paper. The following submission explains why such an exclusion is warranted.

CLOSED LOOP MERCHANT GIFT CARDS VERSUS OPEN LOOP SCHEME PREPAID CARDS

There are a number of key differences between merchant gift cards and scheme based prepaid cards. These differences result in a far better informed and protected consumer who receives much greater utility with their scheme based prepaid card than with a gift card limited to a specific merchant. These differences include:

- **Security**

Most importantly given the recent merchant insolvencies that triggered this review, the cardholder's counterparty risk for the value loaded onto open loop prepaid cards rests with the issuer, not a particular merchant, even if the card carries a merchant's brand.

Once a scheme based prepaid card is purchased, loaded and activated, the issuer immediately becomes liable to the scheme to settle all legitimate transactions up to the card's balance. Since there is a delay of up to 48 hours or more in the issuer receiving loaded funds from the merchant into their settlement account, it is the issuer, rather than the cardholder, who has a counterparty risk with the merchant.

Unlike closed loop merchant specific gift cards, the consumer's exposure for the value of a prepaid card is with the issuer rather than a particular merchant. Such issuers are typically APRA regulated ADIs operating under the Banking Act 1959 and must be principal members of the scheme through which the card transacts (e.g. Visa or MasterCard). The issuer is

obliged to settle all legitimate approved transactions with the scheme to retain their scheme membership.

While the prepaid cardholder may at times be anonymous (for example, with a disposable card) and does not hold a deposit account with the issuing ADI, the responsibility of the issuer to settle transactions with the scheme is no less robust than for debit card transactions against an individual's bank account. The exposure of the cardholders to the issuing bank is underpinned by the strict regulatory and supervisory regime that applies to ADIs, with robust liquidity management protections and oversight to ensure the issuing bank can always meet its liabilities.

- **Single use or reloadable**

Prepaid cards can be single use or reloadable. Single use cards are disposed of once the loaded value has been used, while reloadable cards can be topped up and reused continuously during the lifetime of the card. Merchant gift cards are only single use, sometimes with constraints around even that use, as the Issues Paper has highlighted. Single use prepaid cards therefore look more like merchant gift cards and are, in fact, often used as gifts. The difference is that unlike closed loop gift cards, they are accepted widely, including by online merchants (see below).

- **Merchant neutral**

Since they operate under a scheme such as Visa or MasterCard, prepaid cards can be used wherever the scheme is accepted. This includes most merchants who also accept credit cards, including those selling their own closed loop gift cards.

Unlike a merchant gift card, an open loop prepaid card can continue to be used while legitimately loaded value remains unspent and the card is active, even if it was originally purchased from a now insolvent merchant.

- **Online and foreign purchases**

Open loop prepaid cards can be used to purchase goods and services online. Closed loop gift cards cannot. In fact, consumers often prefer to use prepaid cards with limited balances rather than exposing their personal credit or debit card details to fraud when making online purchases.

In conjunction with Heritage Bank, Australia

Post has recently gone one step further to help consumers protect their personal details when shopping online. If cardholders register their personal and prepaid card details at Australia Post, they can make ebay purchases while providing only their prepaid card number. Australia Post will deliver their purchases by linking the card number to the personal details registered with them.

Prepaid cards also provide an avenue to make online purchases for those who choose not to have a credit card or those who cannot get credit, such as unemployed, borrowers with poor credit histories and some younger or elderly persons. Given that most telephone and online bookings require a credit card, prepaid cards provide high utility for disadvantaged segments of society.

Non-AUD purchases using a scheme based prepaid card can be made, physically or over the internet, even if the card is only denominated in AUD. Such cards are consequently valued by travellers as a vehicle for payment and ATM access to cash that does not expose their credit card or bank account linked debit card to fraud.

• **Consumers protected**

As discussed in more detail below, merchant gift cards are very lightly regulated when compared to prepaid cards. The significant additional regulation of prepaid scheme cards removes, or at worst mitigates, most of the consumer concerns raised in the Issues Paper.

In summary, open loop, scheme based prepaid cards are considerably different products from those producing the consumer issues that the Committee wishes to investigate. Including prepaid cards in the review beside closed loop merchant specific gift cards consequently does not provide added clarity in addressing the primary consumer issues peculiar to gift cards. Their inclusion consequently does not contribute to the development of an understanding of the specific issues that are relevant, and has the potential to result in recommendations that would impose broad-brush additional regulation to highly regulated prepaid cards where strong consumer protection, disclosure and

oversight are already in place.

REGULATION OF GIFT CARDS VERSUS PREPAID CARDS

Both open and closed loop cards are subject to regulatory supervision by ASIC under both the ASIC Act (2001) and the Corporations Act (2001). Generally, under the Corporations Act these types of products are considered financial products and issuers must hold an Australian Financial Services Licence (AFSL), or hold authorisation from a licence holder, in order to Deal or Advise in relation to them.

By holding an AFS Licence, the open loop card issuer is also required to meet the very stringent requirements of Corporations Act regulation including the general conduct and specific licence conditions imposed on licensees, such as; participation in an ASIC approved external dispute resolution scheme (EDRS); having adequate compensation arrangements for customers in case of disputes; having adequate internal dispute resolution practices – all of which are subject to regulatory oversight by ASIC.

This is not the case for closed loop providers whereby under ASIC's powers they have granted class order relief (CO 05/738) to operators of closed loop "gift card" products by exempting them from the need to meet the licensing, conduct and disclosure obligations (as well as the hawking prohibition) set out in Chapter 7 of the Corporations Act 2001.

Unlike the closed loop sector which won some concession from further regulatory oversight, a Financial Services Licence holder (so called a designated service provider – under which open loop cards are covered) is also subject to the regulatory oversight of the Australian Transaction Reports and Analysis Centre (AUSTRAC) and the rules under the various Anti-Money Laundering and Counter Terrorism Financing (AML/CTF) legislative instruments and rules and guidelines as published. AUSTRAC requires designated service providers to; register with AUSTRAC; pay annual levies (from 2012); monitor for and lodge reports on suspicious matters and also be subject to regulatory review.

CONSUMER ISSUES IDENTIFIED IN THE ISSUES PAPER

• Expiry dates

Expiry dates are a mandatory field in electronic payments messages, so all open loop prepaid cards must have an expiry date to operate in the payments system. All prepaid cards, debit cards and credit cards consequently have their expiry dates printed on the card.

Unlike closed loop gift cards, prepaid cards require the provision of a comprehensive Product Description Statement. This document provides consumers with detailed information about the operation, fees and risks associated with the card, including the procedure and cardholder options at expiry.

While a mandated data field that card issuers must impose on every card, card expiry dates also provide issuers with;

- A defined point in time where cards that are no longer used can be deactivated and closed.
- A scheduled time to physically replace the plastic, magnetic stripe and chip to ensure the card's continued uninterrupted performance at merchant terminals and ATMs.
- An opportunity to upgrade the card's capabilities. The incorporation of computer chips onto cards that previously only had a magnetic stripe which are highly susceptible to compromise is an example of such an upgrade.

Most reloadable card programs allow cardholders to roll remaining balances at expiry to a new card that they purchase, ensuring that value is not lost.

Occasionally cardholders can reclaim remaining value at expiry from the card promoter, though this is not common due to the cost and administrative burden this poses for what are typically very small residual amounts. However, it should be remembered that cash can typically be removed from open loop prepaid cards at ATMs and that prior to the expiry date they can be used together with cash to make very small purchases to empty the card's residual value (see below).

• Restrictions on low value use

Given that they operate as scheme based cards, prepaid cards themselves do not have any restrictions

on low value use. However, like credit cards, some merchants impose fees on low value transactions using credit and debit cards, but this is merchant specific and not a feature of the cards per se.

• Terms and conditions in the event of insolvency

As documented in the Issues Paper, there have been a number of recent high profile incidences of merchant insolvencies where gift card holders have been left in line with other unsecured creditors. This situation is unique to closed loop merchant specific gift cards.

Given that open loop prepaid cards are widely accepted, including typically at ATMs, the collapse of a particular merchant does not constrain the use of the card elsewhere. Since funds are held by the issuer who is typically also an ADI, the balance on the card is protected under the Banking Act (1959), with oversight of each ADI by APRA, the banking industry regulator.

• Fees and charges

Different prepaid card programs have different fees and charges. As stated above, a key difference of open loop prepaid cards from merchant gift cards is that open loop prepaid cards require a PDS that clearly and explicitly sets out fees and charges. At many outlets multiple different prepaid card offers from different promoters hang on the same stands side-by-side, allowing comparison by the consumer at point of sale.

If fees are a particular issue for consumers all of these programs have web sites where very detailed information, including the PDS, can be accessed before purchase. This is substantially more likely to occur where the card is bought for personal use than as a gift for the user who has no control over the selection of the card. Reloadable scheme based cards are typically purchased for personal use.

• Limitations on use with respect to retailers that accept the gift card

Scheme based open loop prepaid cards are accepted wherever the scheme is accepted. Such cards, even those only denominated in \$AUD, are able to be used globally, with foreign exchange for settlement of the transaction facilitated by the scheme provider prior to settlement in AUD. The limitation with respect to retailers that accept the card is consequently not an issue with prepaid cards.

- **Receiving change**

Since open loop cards can be used widely, typically including access to cash at ATMs and the ability to supplement the remaining disposable card balance with cash at point of sale, receipt of change is not the issue that it is with merchant specific gift cards.

- **Lost, damaged or stolen cards**

The replacement of anonymous, low value open loop cards that are lost or stolen is problematic since it cannot be ascertained if the claimant is entitled to the card. However, where the cardholder has been identified at point of sale, which is typical of reloadable prepaid cards under anti-money laundering laws, once proof of identity has been provided the normal procedure is to cancel the lost/stolen/damaged card and reissue a new card with the old card's balance.

- **The use of unspent monies and interest accumulated on gift cards**

The issue of unspent monies has been addressed above, with options for prepaid cardholders that are not available to closed loop merchant gift cards.

Prepaid cards are not suitable products for savings

accumulation. Like gift cards, interest is not paid to prepaid cardholders since their balances are typically low and transient, even for reloadable cards.

In this respect they are similar to transaction bank accounts or cheque accounts that typically pay very low or no interest. They are purchased for their convenience or for the security they provide when, for example, making internet transactions, with small amounts loaded for particular purposes.

CONCLUSION

Scheme cards already have robust and stringent consumer protection and product disclosure regulation and oversight in place that is designed to specifically address a number of the consumer related issues raised in the Issues Paper. The insolvency of merchants is also not an issue for open loop cards, since cash loaded onto the card is held by the issuer, typically an ADI, and the card can be used anywhere in the world that the scheme is accepted.

For this reason Heritage requests that CCAAC recommendations be directed solely towards closed loop merchant gift cards, specifically carving out less problematic and highly regulated scheme based cards from the recommendations.

People first.