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24 June 2016

Principal Adviser
Financial System Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email only: CreditCards@treasury.gov.au

Dear Sir/Madam,

Re: Credit cards: improving consumer outcomes and enhancing competition

Thank you for the opportunity to comment on the "Credit cards: improving consumer outcomes and enhancing competition" Paper ("the Paper").

1. About American Express

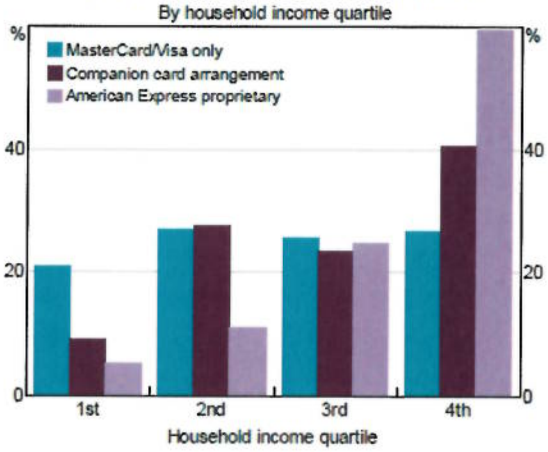
American Express has been operating in Australia for more than 30 years and is a globally recognised payments and financial services provider. Our principal Australian business consists primarily of issuing credit and charge cards and acquiring on our merchant network. We hold an Australian Credit Licence, an Australian Financial Services Licence and subscribe to the external disputes resolution scheme managed by the Financial Ombudsman Service.

2. Premium Nature of American Express Products and Services

American Express offers a premium value proposition across our merchant network and card products. We operate under a value-based pricing model whereby our merchant rate for accepting American Express cards may be higher than for other non-premium merchant acquirers. In return we deliver premium value to merchants, including Card Members who spend on average 46% more per transaction than other card holders. Unlike some other credit card providers, American Express operates primarily in the premium space. Independent data published by the Reserve Bank of Australia ("RBA") shows that the overwhelming majority of American Express Card Members are in the highest household income quartile (see Figure 1).[1]

[1] Published by the RBA in its Review of Card Payments Regulation – Consultation Paper, December 2015 (page 15) see http://www.rba.gov.au/payments-and-infrastructure/payments-system-regulation/regulatory-reviews/review-of-card-payments-regulation/review-of-card-payments-regulation-consultation-Paper.html

Graph 1
Proportion of Schemes' Cardholders*
By household income quartile



* Primary credit card
Sources: Colmar Brunton; RBA

Figure 1

The Paper identifies concerns about persistent revolving and the potential for financial hardship this may cause borrowers, while stating that the higher income earners are generally in a better financial position. The proposals seek to regulate all credit providers uniformly, regardless of differences in performance, including premium lenders like American Express where we maintain best-in-class default rates and significant repayment rates.

There are numerous reasons why customers choose American Express credit card products. This includes access to our premium service, to take advantage of the significant benefits we offer such as flexible payment terms and cash flow management through interest-free payment periods and instalment payment plans. We also offer complimentary insurances, discounts, offers, travel benefits and loyalty programs including reward points. These features and benefits, along with price and interest rates drive competition between credit providers.

3. General Comments on the Paper

In response to changes to consumer credit regulation in recent years American Express has invested heavily in resources, technology and personnel to implement and comply with the requirements. The changes have impacted the amount of credit we can offer to new and existing customers, and how we engage across the customer life-cycle. We support efforts to protect vulnerable consumers from hardship and financial distress, and readily provide assistance to customers experiencing hardship.

The Paper concedes that the majority of Australians use their credit cards responsibly. In our opinion the existing regulations work well and the proposed reforms would have little tangible effect in addressing customer behaviour, including that portion that may suffer financial hardship, or tend to persistently pay only the minimum payment.

Ensuring we issue products that suit the needs and financial capacity of our customers is a fundamental and essential business practise, which mitigates our unsecured lending risk. The vast majority of our customers use their accounts within the assigned limit, repaying on time and usually significantly more than the minimum payment required. As well as best-in-class default rates, requests for hardship assistance are also low.

Further, our experience suggests that the most common reasons that customers experience financial hardship relate to a significant and unanticipated change in personal circumstances impacting their income, including a change in or loss of employment, a serious medical issue or illness, divorce or other relationship breakdown. It is unlikely that the proposed reforms or any other regulation could solve for these situations.

We generally support the proposals to allow electronic initiation of cancellation and credit limit reduction requests, as well as the proposed consumer testing of the effectiveness of various consumer disclosures and notifications, and means of engagement regarding repayment tools.

However other proposals to further prescribe capacity assessment and interest calculations, to prohibit limit increase offers across all credit card users without targeting those customers needing protection would create a significant compliance burden that is disproportionate to the issues being considered.

The Paper grossly underestimates the cost to credit providers to implement the proposed reforms (including the cost to build and test systems and technology, and personnel costs) as well as the ongoing cost to monitor and comply with the requirements. In many cases the purported net benefit of the proposals is entirely unsubstantiated. The Paper also fails to consider the potential for credit providers to significantly change or adapt the way credit cards operate in response to the reforms.

The Senate Economics References Committee's Report[2] indicated the need for regulation to indirectly place competitive pressure on interest rates. However, where the proposed measures drive additional compliance costs, credit providers may simply change the way credit products are structured, including by limiting the number of interest free days and increasing the frequency of statements, potentially increasing the cost of credit cards or maintaining existing rates of interest.

The expectation that these changes will result in beneficial consumer outcomes should also be considered in light of recent reforms to credit cards by the RBA. The RBA reforms focus on improving outcomes for merchants and aim to further reduce revenues to credit card issuers. The RBA expect that following these reforms credit card issuers will either reduce the benefits or increase the cost of credit cards for consumers.

> *"The reduction in interchange fees, especially the cap on the highest credit card rates, is likely to result in some reduction in the generosity of rewards programs on some premium cards. It is likely, however, that there will be only limited changes to other elements of the credit card package (e.g. interest rates, interest-free periods)"* [3]

Together with the proposed reforms outlined in the Paper, the impact of the RBA reforms may not be so limited.

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[2] *'Interest Rates and Informed Choice in the Australian Credit Card Market'* Released 18 December 2015

[3] Reserve Bank Of Australia *'Review of Card Payments Regulation Conclusions Paper May 2016'* Released 26 May 2016. http://www.rba.gov.au/payments-and-infrastructure/review-of-card-payments-regulation/pdf/review-of-card-payments-regulation-conclusions-paper-2016-05.pdf Refer to 'Likely Implications of Regulatory Reforms' on page 47

4. Specific Comments on Proposed Reforms

4.1. Proposal to prescribe a credit limit to be unsuitable if a consumer cannot afford to repay the limit within a reasonable period

We agree that credit cards provide a convenient and flexible tool for customers to manage spending and cover periods of high expenditure, including offering the option to pay a small proportion of the outstanding balance as a minimum payment. The Paper suggests prescribing a credit limit as unsuitable if a consumer cannot afford to repay the entire limit within a reasonable period.

We think attempts to define 'a reasonable period' within the regulatory framework are problematic. Credit cards offer ongoing flexibility for consumers to manage their finances in a way that personal loans do not. This 'one size fits all' approach impacts all credit card providers, not just those with lower minimum repayment requirements or a greater volume of persistently revolving balances, disproportionately impacting the majority of borrowers who manage their credit cards responsibly.

Where such a change has the effect of reducing limits on new accounts and new credit limit increase requests, it will restrict the ability of all borrowers to consolidate debt on other cards, including transferring to lower rate credit cards or utilising balance transfers offers. This would mean that customers wishing to close an account or change credit card provider to reduce their interest obligation may find that they cannot consolidate to one card and therefore retain multiple cards and repayment obligations.

We agree that borrowers should have capacity to pay their debts within a reasonable period. All customers are informed of the possible timeframe and interest applicable where they pay only the minimum payment on their account, as this is outlined in the minimum repayment warning required on credit card statements. Customers should retain flexibility to determine how they pay their accounts without further regulatory intervention.

American Express' minimum repayment requirement for credit cards is higher than that typically set by other credit card issuers, meaning that our customers would reduce their balances sooner than with most other credit providers. In our experience, a vast majority of our credit cardholders choose to pay well in excess of the minimum payment required each month.

4.2. Proposal to prohibit unsolicited credit limit increase offers

The existing regulatory framework requires that all credit limit increases are subject to assessment under responsible lending criteria including with respect to unsuitability and debt capacity. It is misleading to suggest that prohibiting unsolicited credit limit increase offers would have the effect of significantly reducing the incidence of customers receiving excessive limits when limit increases are already subject to a capacity assessment.

Further, under existing requirements credit providers cannot issue written credit limit increase invitations to customers unless they have expressly consented to receive these invitations. Existing requirements also prescribe the way this consent is captured and require that credit providers expressly state and allow that customers can withdraw their consent to receive such invitations at any time, empowering customers to manage their preferences.

Less than four years ago, American Express and all other credit providers made significant investments to comply with the current regulatory framework, including developing, testing and implementing processes and systems to capture and record customer consent to receive written limit increase invitations. The proposal to prohibit such invitations negates both that investment and the informed choice of customers who expressly consented to receive them. The suggested industry costs associated with this proposal do not take into account these initial costs to create and maintain the consent function as currently allowed and prescribed.

4.3. Proposal to standardise the application of interest to the unpaid balance and to the current statement period when an interest-free period is lost

Interest calculation is already regulated under section 28 of the National Credit Code which requires that the maximum amount of an interest charge that may be imposed is the amount determined by applying the daily percentage rate to the unpaid daily balances.

The proposal to reform interest calculations appears to impact when credit providers can waive interest with an interest free period. Generally most credit card issuers will waive any interest on purchases if the cardholder pays their balance in full by the due date. Otherwise interest is charged in accordance with the National Credit Code.

The proposed reform appears to require that interest cannot be charged on purchases until after the statement date and thereafter on an amount below the unpaid daily balance.

For example, assuming that a cardholder opens their account on 1 January, makes a purchase of $2,500, receives their statement on 1 February and pays $250 on the due date of 25 February, the proposal has a material impact on the amount of interest that can be charged to these cardholders.

The following table shows what these cardholders owe each day (Unpaid Daily Balance) compared to the balance on which interest can be charged under the proposed regulation (Proposed Balance for Interest Purposes). In practice these amounts can be far more significant.

January Daily Statement Balances – closing balance $2,500

Date	1 Jan	2 Jan	3 Jan	4 Jan	5 Jan	6 Jan	7 Jan	8 Jan	9 Jan	10 Jan	11 Jan	12 Jan	13 Jan	14 Jan
Unpaid Daily Balance	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500
Proposed balance for interest purposes	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0

Date	15 Jan	16 Jan	17 Jan	18 Jan	19 Jan	20 Jan	21 Jan	22 Jan	23 Jan	24 Jan	25 Jan	26 Jan	27 Jan	28 Jan
Unpaid Daily Balance	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500
Proposed balance for interest purposes	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0	$0

Date	29 Jan	30 Jan	31 Jan
Unpaid Daily Balance	$2,500	$2,500	$2,500
Proposed balance for interest purposes	$0	$0	$0

February Daily Statement Balances – closing balance $2,250 + Interest Charges

Date	1 Feb	2 Feb	3 Feb	4 Feb	5 Feb	6 Feb	7 Feb	8 Feb	9 Feb	10 Feb	11 Feb	12 Feb	13 Feb	14 Feb
Unpaid Daily Balance	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500
Proposed balance for interest purposes	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250

Date	15 Feb	16 Feb	17 Feb	18 Feb	19 Feb	20 Feb	21 Feb	22 Feb	23 Feb	24 Feb	25 Feb	26 Feb	27 Jan	28 Feb
Unpaid Daily Balance	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,500	$2,250	$2,250	$2,250	$2,250
Proposed balance for interest purposes	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250	$2,250

The proposed reform effectively provides cardholders with an interest-free period regardless of what they pay, and a further period of reduced interest balances. This proposal provides a material benefit to those customers who generally pay their credit card in full each month, but occasionally pay less than the full amount. However the proposal provides no benefit to those who pay their cards in full each month. Nor would it benefit those borrowers who always pay less than the full closing balance each month.

This proposal will materially impact the economics of credit cards. Currently interest-free periods are only available to the lowest risk customers, those who pay their balances in full. This proposal requires credit providers to extend the interest-free period more broadly and is likely to cause credit card issuers to review the:

- timing of statement periods;
- offer of interest-free periods; and
- overall pricing of credit cards.

In this way, the likely responses of credit card issuers will impact all credit card customers, including those who always pay less than the full amount each month. This does not appear to have been taken into account in the 'Regulatory burden estimate' table outlined in the Paper, which assumes that credit card issuers will absorb these costs and not make any changes which may impact all borrowers, including those who derive no benefit from this reform option.

The proposal seeks to influence borrower behaviour by regulating credit card interest methodology in a way that benefits a limited portion of borrowers. However the proposal will not benefit that subset of consumers who regularly revolve their balance and incur ongoing interest. Instead it may result in unintended consequences such as significant changes to how credit cards operate generally.

Rather than standardising a changed methodology, an alternative would be to standardise the existing methodology commonly used by credit providers, whereby interest-free periods are maintained so long as the borrower always pays their full closing balance. Standardisation of the common methodology may still support the benefits suggested in the Paper regarding increased competitive tension on interest rates and helping consumers understand the impact of partial repayment. Financial literacy programs could also be standardised under the common methodology to help customers better understand how to avoid interest and maximise the financial benefits of interest-free periods on credit cards.

4.4. Proposal that consumers are provided with simple, electronic options to initiate the cancellation of a credit card and reduction of credit limit

We see some benefit in offering customers easy and technology neutral options to initiate the cancellation of a credit card or to reduce a credit limit, including online, via mobile devices and through automated telephony. We understand that the proposal is to allow the request to be initiated, rather than completed electronically.

We prefer to talk to customers with an outstanding account balance, recurring charges or accumulated benefits or rewards that can be redeemed prior to cancellation. Our experience is that by speaking with them we can service them better, ensuring they understand the implications of closing their account and relevant steps to take, including redeeming rewards points and identifying recurring charges so that customers may make alternative payment arrangements.

By talking to customers we can also identify and address any service issues, and better understand our customer's needs and objectives. We are currently piloting a program that enables customers to initiate the cancellation of their account via our automated telephone service. This process is designed to assist customers who do not have outstanding balances, recurring payments or unredeemed rewards points.

Credit providers would incur technology development and implementation costs to offer these options, which would likely be passed onto consumers in some way.

5. Further Reforms For Testing

American Express supports consumer testing of some further proposed reforms, particularly to assess any real benefit of proposals to increase disclosures and notifications to borrowers.

5.1. Notifications and Disclosures Generally

We note that credit providers currently provide key information to current and prospective customers, including by mandated requirements and in forms prescribed under the current regulatory framework (for example the Key Fact Sheet and Minimum Repayment Warning).

We believe the current system of providing information to consumers is working effectively for the majority of credit card users. We submit that proposals to mandate further widespread disclosures across all credit card customers would drive significant compliance cost for credit providers to implement, with little or no incremental benefit to the cohort that the Paper has identified as most at risk of credit card debt. Such costs would inevitably be factored into the cost of credit card products at the expense of consumers, and would therefore negate any perceived consumer benefit.

American Express has implemented a range of electronic notifications which alert our customers about their account activity, including credit utilisation and payment reminders. We also notify our customers when transactions place their accounts over-limit. We offer a variety of electronic and digital platforms for customers to obtain relevant account information. We allow customers to manage their own preferences in relation to these communications, rather than forcing constant notices. The Paper provides no substantive evidence that mandating push notifications by credit providers would drive customer behaviour and net benefit, yet the cost to develop, implement and maintain such processes would be significant and ongoing.

As a provider of premium card products the majority of American Express' products are designed for affluent individuals who want to take advantage of generous rewards, loyalty programs and other benefits. We also offer zero-fee and lower-rate credit cards as an alternative to those more premium products. Information about these products is readily available on our website and through our customer contact centre, including annual card fees and interest rates. We note that this information can be easily compared across credit providers using various credit comparison services that allow customers to choose credit cards with a range of interest rates, annual fees and other benefits and features.

We do not believe that increased net benefits would be derived from sending consumers information they have not requested and are unlikely to read. Constantly bombarding customers with more information may also result in negative customer reaction and 'information overload', undermining benefit of key disclosures already presented. Vulnerable consumers may obtain better outcomes by further investment in financial literacy programs and debt management services.

5.2. Higher Repayment Options

Card members are currently free to pay more than the minimum due on their credit cards at any time. There are also a variety of payment options to enable customers to pay their account, including by direct debit. In our experience, the majority of our credit card customers choose to pay significantly more than the minimum payment. The cost to build, test, implement and maintain systems which automate a customer's commitment to higher repayment options would be significant yet would provide no more flexibility than currently exists.

5.3. Repayment tools

We support consumer research into effective ways to engage consumers who are consistently making minimum repayments and substantive evidence of the outcomes of such engagement.

6. Summary

American Express agrees that credit cards and associated benefits such as rewards and balance transfers allow customers a flexible way to manage spending and debt. We note that while the majority of customers do manage their credit cards responsibly, some customers experience significant financial distress due to over-spending and under-repayment. In our experience only a small percentage of customers are impacted in this way, and we believe that existing hardship programs sufficiently aid customers in financial difficulty. Further, we believe the proposals may have unintended consequences, create substantial costs to credit providers and may not result in the desired regulatory benefit, particularly when considered together with the recent credit card reforms announced by the RBA.

Yours sincerely,
For and on behalf of American Express Australia Limited

per MS Kratton

Graeme Alexander
Vice President, Head of Compliance and Ethics, Australia and New Zealand