

FINANCIAL SYSTEMS INQUIRY

COMPANY OWNERSHIP OF DINERS CLUB AUSTRALIA

68.2% of DCA

22.7% of DCA

9.1% of DCA = 100%

50% News Corporation

100% Citicorp

60% Fuji Bank
and 6 affiliated companies
40% Japan Travel Bureau

50% TNT
(50% Air New Zealand subject
to Government approval)

- Diners Club Australia is an independent franchise empowered by the Franchisor, Citicorp, to develop regional solutions and products for our valued Australian Card members.
- Our flexibility as a franchise is strongly complemented with access to and backing from some of the largest companies in Australia, Asia and the United States. Citibank is the largest issuer of credit cards in the world.
- Diners Club Australia Card members are able to use their card in 175 countries around the world .
- Diners Club Australia targets the Australian Business Traveller. The company has experienced a near doubling of its card numbers to 300,000 cards on issue, from 1989 to present and sales have increased over 550% in the same period.

THE AUSTRALIAN MARKET

- Regrettably the numbers are "vague" in the credit card market but it appears that Australia has in the order of 30 million plastic payment cards (55% debit cards, 29% credit cards and 16% charge cards). The major growth is currently in debit cards. Countries such as United States of America (information provided later in this Submission) and New Zealand track card numbers closely and are able to provide more accurate information on the total credit card market size in their country.
- The transaction analysis suggests there are some 3.0 million transactions per day with 23% being credit cards, 23% being debit cards, 37% being cash withdrawals at ATM's and 17% being charge cards.
- The average charge size is approximately \$A92 on bank issued cards and \$A179 on Diners Club issued cards.
- Traditional issuers Diners Club, American Express, Visa and Mastercard are now facing new entrants in the Australian market eg. G.E. Capital, Telstra and General Motors.
- AT&T, Discover and JCB are also alleged to have expressed a desire to enter the Australian market.
- Debit cards, both in numbers issued and transactions on cards, have grown rapidly in Australia. Net card growth has been over 750,000 cards in the 11 months ended May 1996 and transaction numbers have grown by over 17% for the same period. Usage has expanded from cheque card to ATM access and now as a global transaction vehicle.
- Store cards have seen the overseas organisation GE Capital purchase Australian Retail Financial Network Services, the largest store card issuer in Australia. If the overseas trend eg Discover card and Sears cards in USA, is followed these, at some future date, are likely to be converted to general purpose cards for the global market.

- Single purpose cards still play a significant marketing role for organisations such as Airlines, Car Hire, Fuel, Taxi and Hotel companies.
- The Australian market has demonstrated there is still room for significant growth in the credit card area however there will be considerable competitive activity to maintain or grow customer loyalty in the future.

THE WORLDWIDE MARKET

- Figures reported in "The Nilson Report" reveal the world market for general purpose cards in 1995 were as follows:

Volume on Global General Purpose Cards

Brand	TOTAL US\$ Billions	CASH US\$ Billions	PURCHASES US\$ Billions
Visa	777.89	189.19	588.70
MasterCard	467.57	112.65	354.92
American Express	161.60	3.11	158.49
JCB	38.10	8.20	29.90
Diners Club	25.41	0.00	25.41
Total	1,470.57	313.15	1,157.42

Purchase volume includes all purchases of goods and services including mail order, telemarketing and all other forms of direct marketing. Cash volume is credit card advances(including balance transfers) and debit card withdrawals.

Of this volume some US\$746 billion is spent in the USA alone. Cash volume distorts the true picture of brand strength, particularly on a global basis where many Visa and Mastercard debit cards are used simply to give consumers access to their own funds on deposit via ATM's. Of note is Purchase volume grew by 17.5% from previous year.

- The number of cards on issue and outlets accepting general purpose cards continues to grow. The reported cards and outlets in 1995 as published in "The Nilson Report" are as follows:

Global General Purpose Cards & Outlets

Brand	Cards million	Outlets million
Visa	446.51	12.10
MasterCard	272.29	12.74
American Express	37.80	4.86
JCB	32.50	3.97
Diners Club	7.10	3.30
Total	796.20	12.74

Visa and Mastercard include both credit and debit cards. Total outlets is the largest figure above because most outlets accept some or all of the cards shown.

- New entrants such as AT & T, Discover, GM and Ford have shown there is no significant barrier to entry and the market while mature competes on switching customer loyalty.
- Worldwide there are 3 billion cards on issue which have magnetic strips. Any of these issuers have the opportunity and may have the desire to enter the financial market.

THE USA EXPERIENCE

The USA alone has US\$745 billion sales on cards of which, US\$609 billion are purchases and the residual is cash. There are 476.7 million cards on issue. The USA has 59.9% of the world's credit, debit and charge cards (general purpose cards) on issue. Also 51% of the turnover \$ volume and 52% of all merchant purchases.

Current USA spending overall is outlined below:

Cash	47.7%
Cheques	35.2%
Credit Cards	13.2%
Debit Cards	0.3%
Other	3.6%
Total	100.0%

DINERS CLUB AUSTRALIA'S OVERVIEW

CUSTOMER EXPECTATIONS

Independent research undertaken for Diners Club Australia reveals that the customer's expectations are:

- Convenience of use
- Excellence in service - solutions to problems
- Simplicity
- Customer needs first, focus on customer first not the profits
- To be treated as an individual
- Accuracy and timeliness in Statements
- Reward for Loyalty

ESTABLISHMENT EXPECTATIONS

Service Establishments desire from the acquirers:

- Speed of payment
- Ease and speed of Authorisation
- Competitive Commission Rates
- Convenience of claim lodgement
- Realistic Floor limits

While much media focus is afforded to the new and emerging technology - Internet/Virtual Shopping etc., it appears much more understanding and trust in the Payment and Delivery Systems will need to be achieved before this will be perceived as a generally accepted means of transacting.

Similarly the development of Smart and Stored Value card technology will need to have convenience perceived as worthy of a price premium if the volume of low \$ value transactions are to see cash and cheques replaced by such technology.

RECOMMENDATIONS

Currently the Australian Financial Service Providers are covered by a range of regulatory bodies including Reserve Bank of Australia, Australian Competition and Consumer Commission, Insurance and Superannuation Commission, Australian Financial Institutions Commission and the Australian Securities Commission.

Additionally consumer regulation is also covered by the Consumer Credit Code, State Credit Acts and State Privacy and Data Protection Legislation.

The Inquiry must, in our view, steer a path ensuring

- the prudential area is appropriately supervised
- consumers, third party suppliers and distributors are protected from abuse of monopoly powers
- the impact of technology, access to the payments system and product innovation enjoy the necessary competition stimuli
- banks and large merged institutions do not use excessive market power at the expense of their customers, smaller competitors and the economy
- foreign entry of corporations needs to be regulated

MERGERS

If the Inquiry recommends Banks, Insurance companies, Telephone, Media and / or IT companies to merge the risk is this may cause a snowball effect whereby the country may end up with one or two dominant financial institutions.

What is the benefit to the consumer from merging? If we look at mergers in other industries the benefits have not happened. Smaller suppliers of Financial Services are concerned the use of market dominance may put them at such a competitive disadvantage as to be economically non-viable. The specific areas of concern include access to the payments system, transaction fees, transfer pricing across products and tying card choice to a range of other products such as home loans.

If one or two dominant financial institutions became a reality this could lead to the Australian Financial System itself becoming destabilised.

IMPACT OF TECHNOLOGY

There is no disputing the rapid pace of technological innovation as applied to the Finance System. The difficulty with the timing of the Inquiry is it appears to be a little too early to meaningfully assess the major changes of some technology and their impact on regulation that may be required. Certainly the combination of Personal Computers linked to Banks and a Global Network (eg IBM, Microsoft) the market could see international entrants from corporations with large capital resources and extensive customer bases (eg Telecommunication companies, Media Groups, Service Utilities) The Internet and the Digital age present many opportunities but as yet are relatively untried in the Financial Industry.

RECOMMENDATION

The Inquiry may choose to recommend this area should be reviewed every two to three years to ensure regulation keeps pace with the changes in this area.

THE DEFINITION OF THE FINANCIAL SYSTEM

Traditional market boundaries are changing. Competitors are changing, companies who were once rivals are now forming alliances and vice versa. Visa and MasterCard are already instructing their Bank card issuers to deny American Express, Discover and Diners Club issuing rights in North America and have failed in Europe.

Card issuers are looking to accept “deposits” from customers on a mutually beneficial basis. The Inquiry will need to ensure its vision of the Finance industry leads to recommendations that balances the Regulatory Structure in a manner that both users of the system and the organisations operating in the system.

The Inquiry should be mindful big institutions who are arguing for deregulation to allow greater freedom and flexibility in responding to global and local forms of competition (current and emerging) have, in the past, not shown the maturity in their customer and third party relationships to suggest we can eliminate regulatory control over their pricing and customer service issues. Details outlined in the section relating to Networks and Commission Rates show evidence of this fact.

RECOMMENDATION

We are recommending a significant widening of the definition of particular finance markets to enable all participants to equally and fairly compete over a full range of services but with some very strong controls concerning competition policy. This should minimise the abuse caused by the monopoly powers of larger players leading to the elimination of the smaller players and should also lead to better customer service and customer value.

PAYMENT SYSTEM

The increasing competition for traditional banking business from both non bank financial institutions and from direct dealing between borrowers and the capital market coupled with the technological change highlighted earlier is radically altering the way Banks can deliver financial services to customers. We need to be certain the Inquiry recommends a regulatory system ensuring the gradual change to electronic transactions through the payment system will deliver improved financial service to customers and third party distributors and also lower costs.

Competitors need to be assured access at a fair price and with fair competition. This means a regulatory body must have the ability to unravel cross subsidies in the pricing of services to ensure competitors are not priced out by the dominance of banks and particularly merged financial institutions.

Two examples in the market today suggest Banks will resort to monopoly powers to thwart smaller competitors and subsequently increase prices. Examples are (A) Electronic Network Transaction Costs and (B) Merchant Commission Rate Policy there are many more examples of this.

(A) ELECTRONIC NETWORKS TRANSACTION COSTS

With speed of Authorisations and pricing of transaction costs so vital to establishments which regulatory body will ensure there is no abuse monopoly powers in pricing transaction costs to third party issuers?

Diners Club Australia, for example, has been offered a wide range of cost per transaction (including communication cost). If there is further concentration of market power Diners Club Australia along with other competitors could be placed in a position of economic non-viability if monopoly pricing prevailed.

What is the process whereby third party users can be protected?

(B) MERCHANT COMMISSION RATE POLICY

Diners Club Australia takes the view that the Inquiry might consider all charges applicable to a merchant relationship need to be effectively identified in a Merchant (Service Establishment) Agreement.

A low commission rate can disguise the real rate by using Transaction Fees, Accounting Fees, Electronic Network Fees, Sign on Fees, No Activity Fees etc. to exact a return much higher than the Commission Rate proffered.

As the majority of Establishments are small businesses the manner the Acquirer arrangements are presented can have a perception price rather than the reality price as the basis for the merchant's decision.

The Inquiry may consider the need to regulate Merchant Contract details as a useful means of eliminating these confusing and possibly misleading pricing policies.

RISK

In considering Systemic Risk alongside prudential supervision; what is the Financial System now and for the foreseeable future?

Given the impact of new technology, the need for consumer protection, product innovation and access to the payments system it is unlikely one mega regulator could have the necessary flexibility and open questioning needed.

The approach should be one of "hasten slowly to move forward more quickly"

The Prudential, Consumer, Competition and Reporting Requirements all need to be accommodated.

REGULATION

Diners Club Australia believes the current regulation of the Finance System is outmoded, fragmented and not providing the control or protection as intended. It is now possible for corporations to "work around" the legislation to provide essentially the same services as a bank and yet not have a banking licence. For example an Insurance company has a product that provides all the services of a traditional bank except Deposit taking and yet does not have a banking licence nor does it need one. It has often been put forward that Australia should aim to become an international headquarters for the Asia Pacific region. To achieve this the Regulation of the Finance System must liberal, friendly, prudent and encourage foreign corporations to relocate to Australia.

The future will no doubt see a further "blurring" of traditional roles where it will be possible to circumvent traditional payment systems. Manufacturing companies, the postal network and the Internet offer possibilities globally to move away from old fashioned banking. Regulations need to be forward looking to account for this change in order to avoid reactive changes brought about due to a crisis.

An example of the issue is what is the role of Visa and MasterCard, will they continue to diminish the value of Bankcard and exert even greater control over Australian issuers? Who will have more say - Visa/MasterCard or the issuer, even if it is one large merged institution?

For Diners Club Australia the current Regulations relating to Credit Providers is confused and different in each State. The proposed Uniform Credit Code is due to be enacted in November 1996 however Tasmania and Western Australia have still not agreed to enact the Code. State based legislation is still subject to an individual State's legislators wish to change.

RECOMMENDATIONS

The Australian Finance System Regulatory Bodies should consider

- Having one body to oversee the prudential aspects of the System. The body would merge the prudential supervision of the Reserve Bank, the Australian Financial Institutions Commission and the Insurance and Superannuation Commission. This would follow the current move of Banks into Insurance markets and Insurers into the Banking market.
- Having one body for consumers to seek advice and support for consumer issues.
- Having one body to oversee issues relating to competition, prices and mergers
- Having one body to oversee the collection and reporting of all information relevant to the Finance System
- In all cases the bodies should be centralised in the same manner as the Australian Securities Commission

PRIVACY ISSUES

There has been increasing public debate in relation to consumers' right to Privacy. Various issues have been raised including

- consumer fears of massive databases containing information such as personal details, spending patterns and demographics
- databases containing incorrect information which may unfairly impact on the consumer, for example the ability to obtain credit
- consumers desire to ensure the information is not misused, for example the information may be fraudulently used or use of addresses for mail lists

The need for Privacy needs to be counter balanced with the need for appropriate access for information for a Finance or Card company. Diners Club Australia has an ongoing requirement for access to a consumer's credit information during their time as a cardmember whether they are a person or a corporation. Such information is required in order to make decisions on continuing credit worthiness or possible fraudulent activity.

The USA experience suggests that unless these issues are clarified Finance and Card companies may become the subject for increasing litigation from dissatisfied customers.

RECOMMENDATIONS

The Australian Finance System needs to :

- Ensure clear guidelines are available for service providers who require ongoing information relating to consumers
- Ensure there is an ability to share information between other organisations in certain situations
ie For a card company the issue may be unusually large \$ transactions needing information from a third party relating to ongoing credit worthiness or potential fraudulent activities
- Ensure there is a secure process for consumers to be able to correct information on a database

FRAUD

It is estimated the cost of Fraud in the Australian market was \$120 million last year and is growing at rate of 45% per annum. The management and control of Fraud losses is a major area of concern for any card company operating not only in Australia but worldwide. Australian law enforcement, prosecution and sentencing appear to be totally inadequate to deal with this growing problem. The worldwide trend links credit card fraud to organised crime, gambling and drug usage.

The process of managing fraud loss involves Prevention, Detection and Investigation.

Prevention

- prevention of Fraud often involves staying one step ahead of mostly international gangs of counterfeiters' and criminals' ability to replicate cards or work around security measures
- elaborate and expensive card systems using magnetic stripes, photographs on cards, etc have been developed
- both cardmember and merchant awareness programs aimed at educating users to the steps to take to prevent Fraud
- industry networking to share information worldwide. The International Association of Credit Card Investigators provides much needed regular updates and conferences on Fraud trends.

Detection

- Detailed reports are required to ensure fraudulent activity is detected as early as possible. This is a critical element to the management of Fraud as there is an opportunity for organised criminal gangs to make significant sums very quickly unless detected early.

Investigation

- Diners Club Limited maintains its own Security Team, with a number of Senior Fraud Investigators, however it is essential to maintain a close working relationship with various Law Enforcement Agencies, both within Australia and worldwide.

RECOMMENDATIONS

The Australian Finance System Regulatory Bodies need to

- Understand the need for effective sharing of information between the Service Providers and the Law Enforcement Agencies in relation to Fraudulent activity.
- Ensure the new forms of technology entering the payments system, such as Smart card, have taken the appropriate steps to maintain the safety of funds.
- Ensure Australia takes appropriate steps to co-operate with other international agencies.

REPORTING

Diners Club Australia believes no decisions relating to the effects of changes to the Finance System can be made unless the appropriate facts are available. This is especially so in relation to the effect of creating so called "mega Banks" or changes from new technology. The current system of reporting in Australia is fragmented and incomplete. Registered Financial Institutions, usually Banks, report to the Reserve Bank of Australia, Insurance companies report to the Insurance and Superannuation Council and other information is gathered by an assortment of other agencies including the Australian Bureau of Statistics and the Prices Surveillance Authority. Information requested is not uniform nor is it complete. Even the very useful Prices Surveillance Authority reports provide only part of the total picture. There are no statistics available on the value of cheques passing through the system, the number of payment cards issued in Australia, the value of payments passing through the financial system and so on. Countries such as United States of America and New Zealand collect such information and are able to report and therefore speak with authority in relation to trends, the possible effects of changes due to mergers and the consequences of technological changes.

Diners Club Limited Recommendations

The Australian Finance System Regulatory Bodies need to:

- Centralise the system of collecting information for the Finance System
- Establish clear definitions for information being collected. For example the Australian Card Industry has a multitude of cards issued including
 - Bank issued credit cards - some interest free some not interest free
 - Bank issued debit cards
 - non Bank issued credit cards
 - Charge cards - no extended credit period
 - Retail credit cards - useable at one retail chain
 - Single purpose cards - useable for Airlines, Taxis, hire cars, hotels etc
 - Fuel cards - useable at one or more service station outlets
- Establish what are the products and what reporting is required to give the complete picture.
- Information collected is available to both the Regulatory bodies and the public.

SUMMARY

Diners Club welcomes the opportunity to present this Submission. We would welcome any request for further information or to expand our views as presented to the Inquiry Committee.

Contact points

Mr Grant Halverson
 Managing Director
 Phone number: 03 9805 4566
 Fax number: 03 9805 4455

Ms Jennifer Taylor
Special Projects Manager
Phone number: 03 9805 4443

Diners Club Limited
1193 Toorak Road, Hartwell Victoria 3124