

**Parliamentary Joint Committee on the
Australian Crime Commission**

Inquiry Into Cybercrime

Submission No:16

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Submission To the Joint Committee On The Australian Crime Commission

Introduction

This submission is forwarded at the suggestion of the Australian Banking Industry Ombudsman, Mr Colin Neave, who felt the issues might be of interest to the committee. This is not meant to imply that Mr Neave necessarily agrees with the opinions of the author.

By their failure to implement proper security to prevent known frauds, banks are aiding in the commission of credit card fraud. They then complete the fraud by extracting the money from the unwitting victims, credit card merchants.

The Issues

1. Banks market credit cards as a safe means for merchants to accept payment from customers.

Representations are made to merchants with such claims as “cleared funds in your account the next day” and “much safer than accepting payment by cheque as it cannot bounce”.
2. Merchants are given operating instructions and told that payment is guaranteed provided they follow the instructions correctly. Such claims are also implied in writing in bank marketing material.
3. If a merchant is unfortunate enough to be targeted by fraudsters and conduct a transaction, entirely in accordance with the instructions provided by his bank, the bank will, after a protracted process of correspondence with the merchant, charge back the transaction to the merchant.
4. The banks do this on the basis of certain terms in the Merchant Agreement. When signing up as a merchant the author was assured that these terms were meant only to protect the bank from merchants engaging in fraud.
5. The merchant agreements also oblige merchants to accept payment by credit card when any other means of payment would be acceptable. This makes it a breach of the merchant agreement for a merchant to do otherwise than accept payment by credit card.
6. When a transaction is processed manually, except for small transactions under the ‘floor limit’, the merchant phones the banks authorisations centre for approval and is quoted an authorisation number.
7. When a transaction is processed by EFTPOS, in all cases the EFTPOS machine will print out a voucher indicating a transaction is APPROVED or declined for some reason.
8. Nowhere in the merchant agreement are terms such as AUTHORISED or APPROVED defined to have special meaning and merchants assume that when the bank has authorised a transaction the words have their common English meaning and the bank is accepting responsibility for the transaction.

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9. Banks and the credit card companies such as Mastercard and Visa do not operate a safe and secure credit card system. They knowingly fail to implement security procedures to defeat known credit card frauds. They do this in the knowledge that thus far they have been able to transfer the cost of their negligence onto merchants. Evidence to this effect was given in the Victorian County Court by a former bank investigator.
10. When banks become aware of credit card scams targeting a particular group of merchants they fail to either notify the target group of merchants promptly or take other action to protect them such as monitoring their accounts for unusual and possibly fraudulent activity.
11. By their inaction and neglect, banks provide an essential component in many credit card scams. They are in effect, knowing accomplices and play an essential role in the extraction of money from innocent targets of organised crime gangs. If they bore the cost of the weakness of their security they would be under strong pressure to implement appropriate security measures.
12. No authority appears to be willing to investigate these matters and take any action against banks for their wilful neglect.
13. The author and his legal representatives made attempts between 1996 and 2002 to have the ACCC investigate the banks, believing that their behaviour, as described above, was unconscionable and that the banks had engaged in misleading and deceptive conduct in not revealing to merchants the risks that the Banks, under their interpretation of their Merchant Agreements, were exposing their merchants to.
14. The solicitors for the bank involved with the author admitted in a letter to the author's solicitor that corrupt employees of another bank may have been involved in the fraud the author was a victim of. The author had no idea he was exposing himself to such risks when becoming a credit card merchant.
15. The author also has documents, obtained under discovery, that indicate banks considered placing a clearance time on credit card transactions but dismissed it for commercial reasons. In effect the clearance time on credit card transactions is 6 months as within that period the banks may chargeback a transaction to a merchant. This fact is not revealed and would be a major deterrent to merchants.

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16. The joint RBA/ACCC paper 'Debit and Credit Card Schemes In Australia – A Study of Interchange Fees and Access', October 2000 states on p47 " Provided merchants follow agreed procedures, they are guaranteed payment. Issuers incur a number of costs in providing this guarantee, including the cost of fraud (and its prevention), credit losses and various risk control costs, such as authorisation of transactions and investigation of specific transactions."

It continues on p48. "In addition, it is not clear that fraud costs incurred by issuers should be borne by all merchants. Credit cards are increasingly being used over the telephone and Internet for purchases and payment of utility bills. Such 'card not present' transactions do not usually attract a guarantee of payment because merchants are unable to verify signatures. Although payments may be authorised by the card issuer, the risk of fraud is often borne directly by the merchant, to whom fraudulent transactions may be charged back if the cardholder disputes a transaction. In many countries, credit card schemes recognise this in a lower interchange fee so that merchants do not pay twice – once for the purchases directly charged back to them, and a second time to cover issuers' fraud losses in respect of other merchants for which payments are guaranteed. In Australia, by contrast, 'card not present' transactions attract the higher interchange fee of 1.2 per cent for transactions that do not qualify as electronic. The study can see no logical basis for this practice when fraudulent transactions can be charged back to the merchant; it has some merchants paying twice."

No such distinction between card present and card not present transactions was made in the author's Merchant Agreement. Whether some banks issue different agreements is not known. In either case, banks appear to have little intention of recognising the existence of a payment guarantee in practice.

17. The author is prepared to make available all correspondence between him and the ACCC and all of the supporting documents supplied to the ACCC such as Merchant agreements, operating instructions etc. and to give evidence to the committee if called upon to do so.

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Conclusions

Banks are dishonestly enticing Credit Card Merchants into an arrangement where they are, according to the Banks view, exposed to all of the risks of an insecure credit card system that the Merchant has no control over, and failing to inform Merchants of these risks.

Banks are failing to implement available measures to counteract known credit card scams, preferring to rely on their ability to coerce Merchants into bearing the costs of any resulting fraud.

Banks use highly misleading terms like AUTHORISED and APPROVED in relation to credit card transactions to which they attach a particular meaning that is not defined in their documents. Effectively, should a dispute arise, they define these terms to mean almost nothing.

The organisation charged with administering the Trade Practices Act, which includes dealing with matters such as unconscionable conduct and misleading and deceptive conduct appears to regard banks as 'untouchable' and has steadfastly refused to investigate any of these issues.

Recommendations

The committee should seek answers from the ACCC as to why it so steadfastly refuses to examine these matters, including such absurdities as claiming that the author is the only merchant who has ever complained about this issue. The author has provided the ACCC with a list of names of merchants similarly affected.

The committee should consider recommending specific legislation to give protection to Credit Card Merchants in circumstances where they have complied with all conditions and operating instructions specified by their bank.

Banks operate the credit card system and profit enormously from it. They should bear full responsibility for the security of their system and therefore have the incentive to improve that security as much as possible.

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