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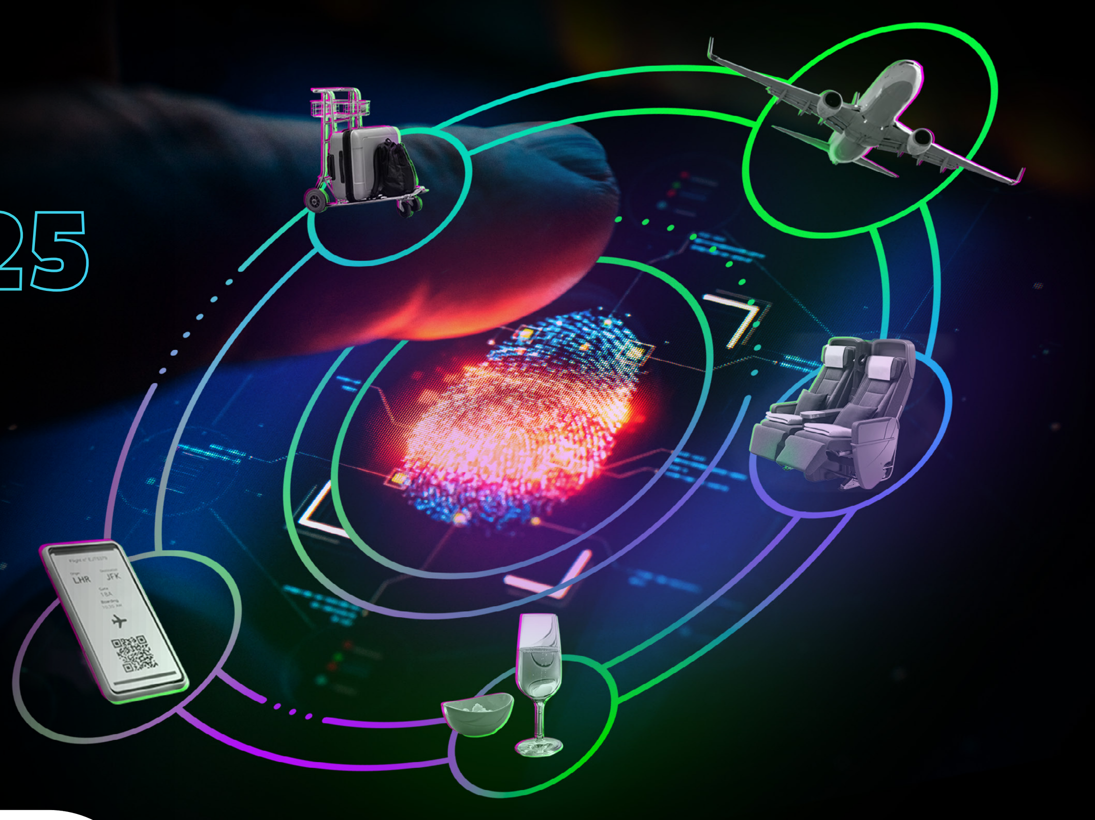
AIRLINE & TRAVEL PAYMENTS 2025

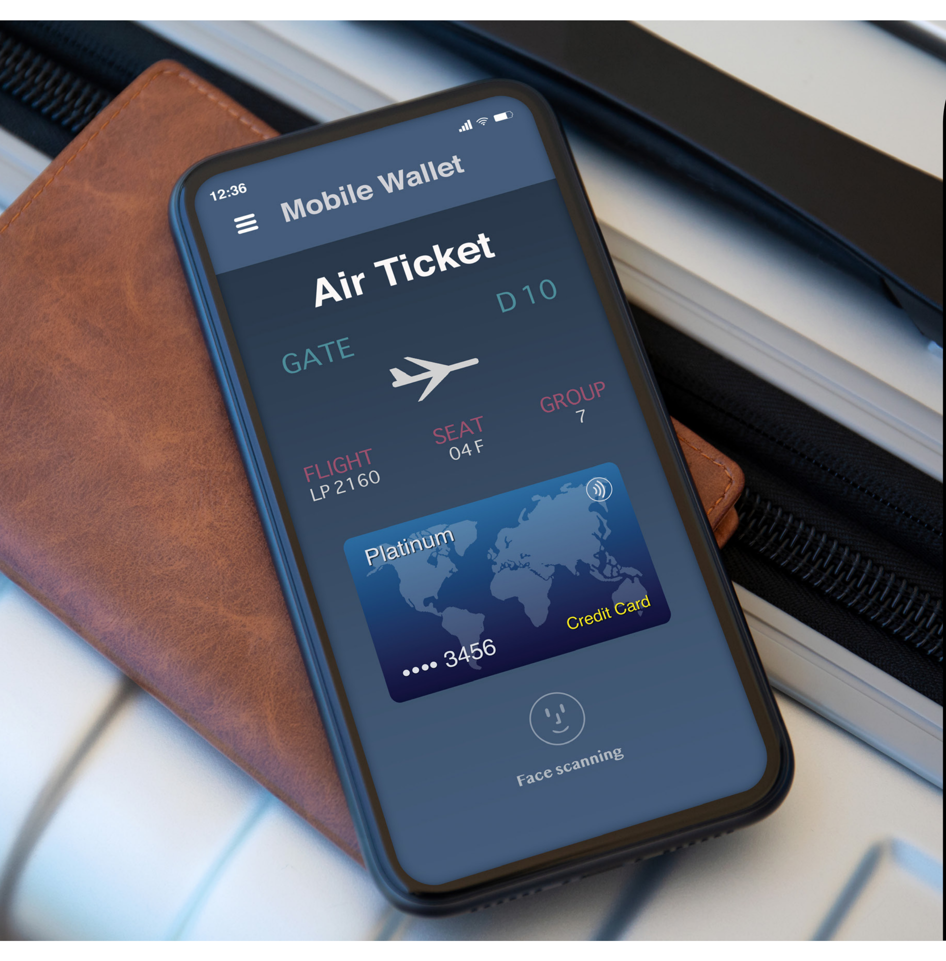
Payment Risk

PAYMENTS 2025



How acquirers can mitigate commercial risk and what this means for the air travel industry

There's a good reason why credit cards still enjoy relatively high usage in the airline industry (approximately 70% of retail transactions)[1]. Alongside potential loyalty benefits, such as frequent flyer miles and travel insurance packages, credit cards also offer a degree of financial protection to cover the customer if they don't receive the service that they paid for. Customers are protected from worst-case scenarios, such as flight cancellation, bad passenger experiences (at the fault of the airline), or even an airline going out of business. Unlike some other forms of payment, credit cards give the passenger the option to claim a chargeback.



Cardholder's gain, acquirer's pain

While this protection is a positive benefit for the passenger, it has major implications for other players across the airline payment world. Ultimately, someone is responsible to cover this risk; the cardholder must be paid if the chargeback claim is deemed valid. Under normal circumstances, the acquirer would hold the airline accountable for a chargeback and deduct the refund amount from other sales. However, if the airline is no longer in business and there are no further sales to offset the chargeback amounts, the responsibility falls on the acquirer. Simply put, the acquirer is obliged to pay.

In turn, this means the acquirer is potentially liable for all un-flown tickets, as well as tickets that have been converted into refund vouchers. This is something the industry has seen plenty of, particularly during and in the aftermath of the pandemic, and can amount to tens of millions of dollars for an average-size carrier.

Travel agents know the benefits of virtual cards

It's not only travelers issuing chargebacks, but sellers too. Travel agencies have learned to appreciate the value of chargebacks for unrendered services on their cashflow. Too often during the pandemic, agencies were forced to wait for refunds from the airline for canceled flights, while having to reimburse the passenger immediately. Virtual Credit Cards (VCCs) provided travel agencies with a more cashflow-friendly way to settle; by acting as the merchant of record, agencies are protected by similar rights to direct customers. With most VCC programs, the travel agency can submit a chargeback request and are able to mitigate against an airline's default or service disputes. They are not able to do this using the traditional way of settling funds between travel agencies and airlines - the IATA BSP (Billing and Settlement Plan) cash process. For the airline's acquirer, this means travel agency VCCs can be viewed similarly to regular passenger cards in that they bear a default risk until the ticket is flown.

How can acquirers mitigate this risk?

As we have witnessed in history, an airline becoming insolvent could also cause the acquirer to fail. Subsequently, the default risk moves up the chain to the card schemes, who would then have the final obligation to pay out cardholder chargebacks.

Acquirers (and card schemes) don't take this level of risk lightly. From the outset, if the acquirer is not deemed financially strong enough, the card schemes will limit the level of trade they can conduct with the airline. For the most stable and reliable carriers, acquirers are more likely to pay out with almost immediate effect, although they retain the right to impose risk protection measures at their discretion.

- **Deposits –** these can be paid in cash, upfront by the airline, or via pre-agreed amounts withheld by the acquirer. Depending on their risk appetite, airlines may need to cover the full Un-flown Ticket Value (UTV) of the airline, which may be in the value of millions, or in some recent cases, billions of dollars. More often, acquirers feel comfortable with partial coverage. These amounts can be agreed at the beginning of the contract and are updated either periodically or adjusted regularly according to seasonal fluctuations. Alternatively, they could be more dynamic, for example paying out as flights are flown. The latter requires smart reconciliation tools (provided by brands such as Actuary) that match payment transactions with notifications of lifted tickets.
- **Trusts –** although these work similarly to the deposits outlined above, instead of the acquirer holding the funds, money is deposited into a trust account with an independent third party until the airline has provided the promised service. In case of any insolvency, the trustee refunds the acquirer with money from the trust account.

> "The impact of the pandemic has taught us that collaboration between the links in the airline card payment processing value chain is more important than ever before. Transparency about exposure caused by cardholder protection, updated and reported on a daily basis, in combination with pro-active and open communication between stakeholders will be key in restoring the balance in the ecosystem, ensuring that there will be sufficient acceptance supply to meet the returning and growing demand for both B2C and B2B card transactions. With Actuary we have introduced a community-driven, trusted 3rd party that acts as data exchange and intermediary, supporting merchants, acquirers, and card schemes in monitoring and managing credit risk for deferred delivery products and services."
>
> **Maarten Alleman, CEO at Actuary**

- **Guarantees –** these can be provided in the form of a bank guarantee, in which the bank promises to cover funds in case of bankruptcy, or a guarantee provided by the airline's owners, including governments, holding organizations, and parent airlines.
- **Insurance –** Failure or insolvency insurance provides a source of contingent funds to repay cardholders if an airline fails. However, insurance has not yet become widely adopted as a core risk mitigation tool because of a severe lack of capacity available to the Airline & Travel Payments market from traditional insurers.

> "Insurtech marketplaces, like AkinovA, are developing the infrastructure to introduce new sources of alternative, long-term investment from the capital markets to underwrite insolvency protection insurance products that provide a direct replacement for holdback deposits or guarantees. By leveraging first- and third-party data, cover can be tuned to the exact risk exposure, on a flight-by-flight basis or up to the total default risk of an Airline or Travel Agent. Insurance transfers the risk away from the acquirer and releases liquidity restrictions on the merchant."
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> **Martin Cunnison, Client Director at AkinovA**

Despite having all these mechanisms in place to minimize risk, understanding and managing exposure still remains a monumental task that many acquirers aren't anticipating or prepared to take on. A few large bankruptcies, including Air Berlin and Thomas Cook, have burned the industry's confidence, while the uncertainty of the pandemic exacerbated this risk. As a result, many financial players have moved out of the travel space or reduced their activities. Understandably, the few acquirers that are still in the business have tightened their risk mitigation processes.

What does this mean for the airline world?

Although alternative payment methods are on the rise, credit card flows are still a major form of income for every airline. For the twelve months preceding October 2022, around 85% of customers paid for airline tickets using payment cards, a trend that was accentuated by the pandemic as more customers switched to online distribution channels . Travel agents are amplifying the challenge by moving from BSP cash payments to virtual cards. Now more than ever, airlines need to find a suitable acquirer.

Finding the right acquirer for their business is vital but can be a challenging task. Choosing a strategic partner that understands the complexity of the airline world and can fairly evaluate the commercial risk will help to balance the airline's need to mitigate acquirer risk whilst also managing cash flow.

Building and maintaining a good relationship between the airline's finance department and the acquirer's risk team is paramount to minimizing the threat of sudden increases in deposit requirements during financially difficult times. Today, having a multi-acquirer strategy is likely a more common and sensible move, given the inherent risk associated with one acquirer managing the entirety of an airline's card funds.

Click to watch

We invited a group of leaders across airline and travel payments to discuss key trends and opportunities shaping the industry. Here's what some of them had to say about Payment Risk:

Worldpay for Airlines

At Worldpay from FIS we work with more than 100 airlines. For over 30 years we've built our expertise to evaluate, understand, and manage airline acquiring risk. Our expert teams, supported by an extensive set of risk management tools, work relentlessly to find an optimized approach, tailored to each individual airline. From low-cost to network carriers, private aviation, and beyond, we're here to support travel businesses across the globe in achieving their payment goals.

> "Worldpay from FIS have not only supported our airline customers through a turbulent period but also expanded our airline portfolio over the last 2 years. We work to understand each airline individually and find creative ways to structure a deal that is beneficial to both parties. With such a large airline customer base, we have extensive knowledge and understanding of the sector and go to great lengths to understand each airline's risk proposition. As a risk function, we partner and support our airline customers."
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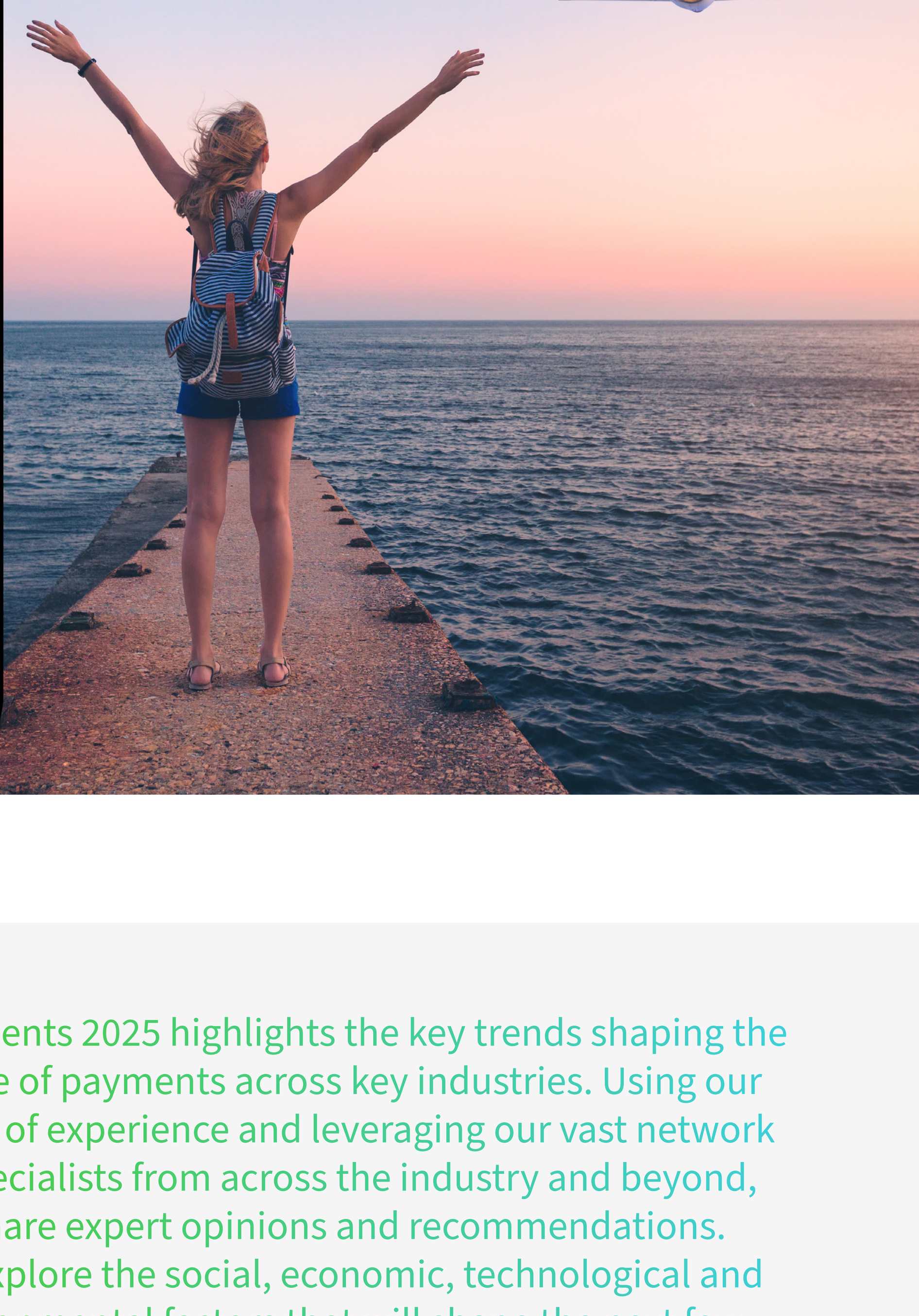
> **Neil Hilton, Head of Large Credit UK & EMEA, Worldpay from FIS**



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[1] McKinsey & Company, September 2022 [2] ARC, Airline Sales Statistics

Get in touch with us today

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Payments 2025 highlights the key trends shaping the future of payments across key industries. Using our years of experience and leveraging our vast network of specialists from across the industry and beyond, we share expert opinions and recommendations. We explore the social, economic, technological and environmental factors that will shape the next few years, so we can help you prepare for tomorrow.

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