The EU Work on Payments

W3C – Workshop on Web Payments
Paris, 24–25 March 2014

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The views expressed are purely those of the author and may not be regarded as stating an official position of the European Commission.

Outline

- Background
- Competition cases
- Aim of the legislative proposal
- What do we propose?
- What do we expect?

Background

- Retail payment business accounts for **up to 25% of total bank revenues and 1% of EU GDP.**
- The merchant service charges (**MSC**) paid by retailers ≈ €13 billion annually in the EU. About €10 billion are **Interchange Fees.**
- This, in spite of the value of payment card transactions in the EU increasing continuously, from **7.4% in 2000** to **17.4%** of the EU GDP in **2012**.
- At the same time, **online shoppers** in Europe expected to increase from **157 million in 2010 to 205 million by 2015.**
- Cards more or less ubiquitous: **1.45 per capita** in EU, **0.9** debit cards and **0.55** credit cards.
- No sign of MIF rates decreasing (except in response to regulatory pressure or competition enforcement) as a result of scale effects or efficiency

MasterCard and Visa proceedings

MasterCard

- December 2007: prohibition decision
- April 2009: Unilateral undertakings reducing MIFs for cross border transactions to 0,20% (debit cards) and 0,30% (credit cards) and enhanced transparency
- May 2012: Judgment General Court, appeal rejected, higher appeal to CoJ
- January 2014: Opinion AG advising to reject appeal

Visa Europe: Commitment offers

- December 2010: Commitments Decision regarding Visa Europe's debit card MIFs (cap at 0.2%)
- February 2014: Commitments Decision regarding Visa Europe's credit card MIFs (cap at 0.3%) (reduction of 40/60%)
- Cross-border acquiring: reform of Visa's system in such a way that retailers will be entitled to application of the reduced cross-border inter-bank fees when they make use of the card acceptance services of a bank in another Member State.

MasterCard II, Visa Inc

- Proceedings continue for inter-regional MIFs and cross-border acquiring

Level of MIFs in Commitments

- Based on merchant indifference test (MIT) – net benefits to merchants from card acceptance
- 0.2% and 0.3% based on central bank studies
- Carried out a detailed study into the cost of cash and card acceptance for merchants in 10 countries. 254 merchants participated
- Preliminary results published in February 2014: MIFs of 0.11% debit and 0.15% credit for the merchants in study
- But only large merchants and only face-to-face transactions. So believe results fully compatible with 0.2% and 0.3%.
- Will prepare final report by summer.

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E-payments case against the EPC

- 2011 opened formal proceedings against the EPC for its work on the e-payments framework
- Normally standardisation pro-competitive, but in this case concerns about exclusionary effect on non-bank epayment providers
- Worked with EPC to prepare pro-competitive standard, but EPC chose to stop its work
- Closed case in 2013 and said:
  - Will monitor epayments market to ensure exclusionary action not taken at national level
  - Will propose legal base for TPPs

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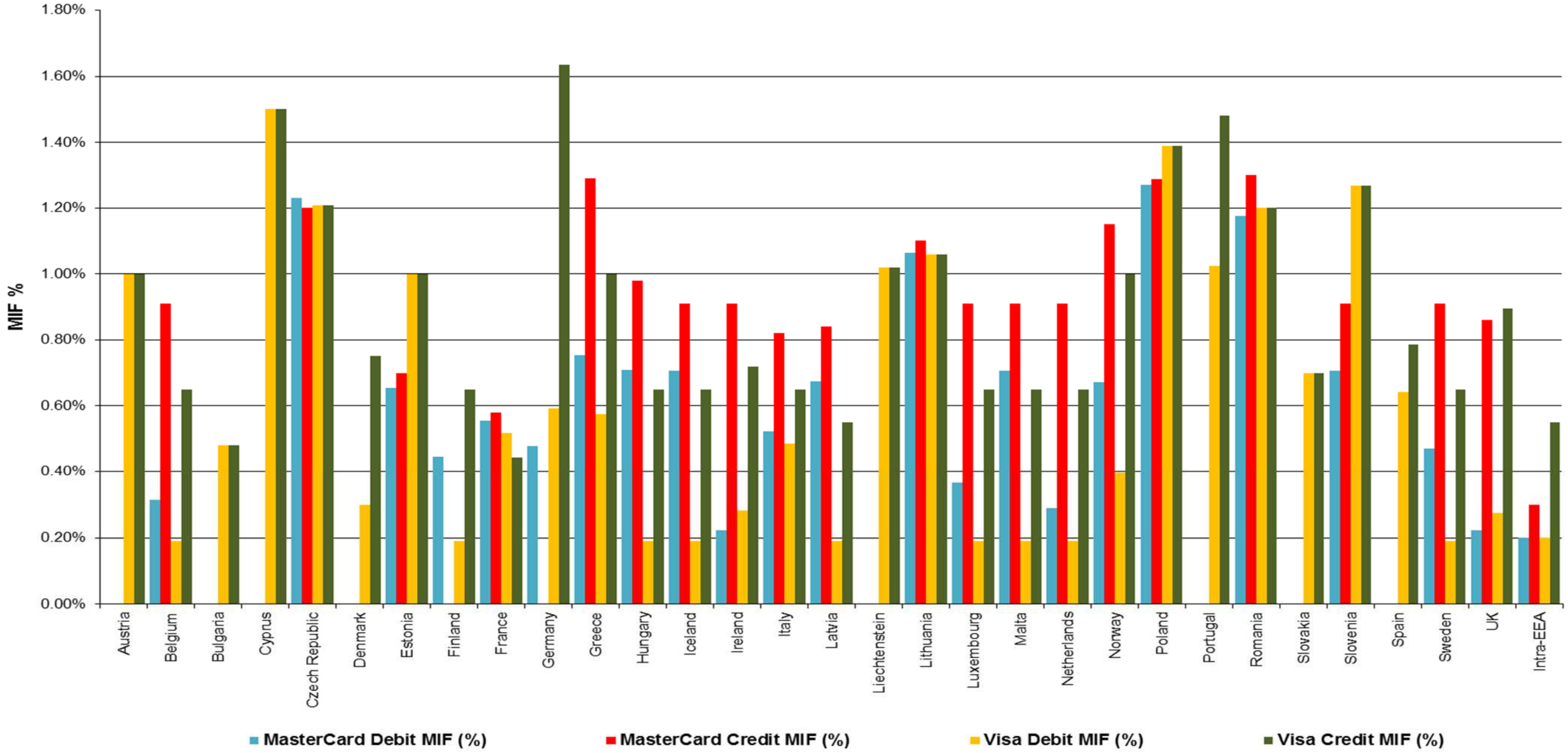
What is the problem with Interchange Fees?

- IFs are hidden fees based on collective agreements between banks that create a ‘floor‘ in the fees banks charge to retailers
- Retailers pass these fees on to consumers
- Harmful effect enhanced by
  - ✓ Incentives given to cardholders to use highest revenue generating cards
  - ✓ Network rules restricting transparency
- No indication that consumers receive appropriate share of efficiency gains, also taking into account
  - ✓ 'Business stealing' effect on retailers
  - ✓ Reverse competition between schemes.

Effects on Internal Market

2013 (Estimated) Weighted average domestic MIF of Visa and MasterCard by country - Consumer Cards



New Entrants and Innovation

- ATMs and internet banking
- PayPal
- PayFair
- Monnet
- Ideal and MyBank
- Sofort

Need for a regulatory initiative

- Competition enforcement cannot deliver a level playing field and cannot act fast ("last mover advantage")
- Member States enforce competition rules and start to regulate: need for consistency
- Want legal base for non-banks (TPPs)
- Want internal market in payments with effective competition for consumers, retailers and successful PSPs and card schemes

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Aim of the Proposal

- Promote consumer welfare
  - Reduce excessive fees to merchants and consumers
  - Increase choice in means of payment
- Promote competition
  - Address collective setting of prices and ensure benefits of any efficiencies passed to consumers
  - Limit barriers to competition and transparency for merchant (blending, HACR, transparency, co-badging)
  - Reduce barriers to entry
- Promote innovation
  - Reduce interchange fees
  - Reduce barriers to entry

What does the Commission propose?

- Regulating fees of 'must take cards'
  - Cap cross-border transactions made by cardholders from other Member State ('cross border fees' accepted in commitments)
  - Address fragmentation of Internal Market by liberalising cross-border acquiring, allowing retailers to benefit from cheaper acquiring services from acquirers established in another Member State
  - Cap for cross-border transactions and cross-border acquired transactions: 0.2% (debit cards) and 0.3% (credit cards)
  - After two years, cap fees for domestic transactions

More Effective Cards Market

- Provisions leading to more competition, more effective pricing signals and empowerment of retailers and consumers
  - allowing merchants to refuse cards
  - allowing surcharging if MIF not regulated
  - easy identification of expensive cards
  - for co-branded cards: choice of brand with consumer and retailer
  - separation of processing and scheme management

Legal Basis for TPPs

- Open market for TPPs provided they are secure
- Conditions
  - Supervision and licensing
  - Identification of TPPs if used in transaction
  - Limited access (receipt of payment order and adequate funds)
  - No storage of confidential data or credentials
  - 'Strong authentication'

State of Play regarding the proposal

European Parliament

- Voted in ECON Committee on 20 February:
  - MIF caps after 1 year; 7 cent max for debit MIFs; cover commercial cards; cross-border acquiring at rate of acquirer's country
- Plenary Vote on 2 April

Council

- Work ongoing under Greek Presidency

'Trilogues'

- Under Italian Presidency in Autumn?

What do we expect? the debate

- Will retailers keep all the savings for themselves?
  - Consumers already pay through the incorporation of IF in the retail prices, and banks are less likely to pass on the benefits of the IF to their account holders than merchants to their clients.
  - Some evidence of pass on of savings – even if analysis of pricing trends tricky
- Will small retailers suffer while big ones gain?
  - Small retailers benefit from caps on IFs. Increased transparency will help small merchants negotiate better prices for MSC.
- Will innovation be stifled?
  - IFs prevent new players and business models from entering the market.
  - Different interchange fees = fragmentation of the EU market into 28 national markets. This makes it difficult for successful innovations to spread throughout the EU.

What do we expect II?

- Will decreasing IFs call into question cash displacement and the fight against fraud/the black economy?
  - A decrease of high interchange fees seems to lead to a higher acceptance of cards, e.g. in Spain
  - In countries with low MIFs cards usage is higher, e.g. Denmark and the Netherlands
- Will banks suffer from decreased IFs and find other sources of revenues?
  - Impact likely to be mixed: increased card usage + cost savings (cash handling, lower IFs to be paid for ATM cash withdrawals)
- Will TPPs be safe? And how will they impact the market?
  - The conditions in PSD should be sufficient to ensure safety equivalent to banks
  - Cannot predict impact on market, but good for competition and innovation and expect good for consumers

Effect of Limiting Excessive Interchange Fees