PAYMENTS EUROPE

PAYMENTS EUROPE COMMENT

EY/CE study on the application of the Interchange Fee Regulation

This paper aims to provide a high-level commentary by Payments Europe on the study commissioned by the European Commission to EY and Copenhagen Economics (CE) on the application of the Interchange Fee Regulation (IFR), published in March 2020.

Summary

- Payments Europe agrees with the overall conclusion made in the EY/CE study; that the IFR has met its objectives and that there is no need for further legislative changes at this stage
- Concretely, we specifically agree that;
    - Consumer interchange fee levels should remain at current levels
    - Commercial cards should not be included in the scope of the IFR
    - There is no need to further regulate other fees within the 4-party card scheme model
- However, we also note that the study has deficiencies in relation to the data collected from domestic schemes and smaller retailers and note that this may have impacted some of the results of the study
- Finally, we argue that consumers have not been given an effective choice of payment brand at PoS and online

Consumer interchange levels

We agree with the study's conclusion to keep consumer interchange at current levels

The study recommends keeping the consumer interchange caps at the current levels (0.2 bps for debit and 0.3 bps for credit). Payments Europe agrees with this assessment and believes there is no need to change the levels. There are several reasons behind this and why it would be harmful to lower the levels any further. Firstly, the decrease in interchange fee levels has led to billions of savings for European retailers and the caps have thus led to its intended consequence. Secondly, lowering the caps further would have detrimental effects for consumers who are likely to have to pay more for their banking and payment services. We note that the study concludes that the current caps have not led to consumers paying more for their banking services. However, there are examples of issuers who have been forced to raise fees or decrease benefits linked to cards due to the interchange revenue losses. The current caps have already severely squeezed the margins of card issuers and any further reduction is likely to result in the revenues from interchange falling well below the cost of servicing a card user.

The study recommends collecting further evidence about the effects of maximum fee amounts. In our view, a maximum fee amount or absolute cap would severely undermine the economics of the 4-party card scheme model and in particular higher value transactions with 4-party card scheme cards would be loss making. This would constitue a competitve disadvatage compared to other, unregulated payment methods.

Commercial cards

We agree with the study's conclusion to keep commercial card products exempt from the IFR

The decision to exempt commercial cards from the interchange fee caps was made primarily because they have a very limited market share and were not reasonably expected to serve as a substitute for consumer cards. Commercial cards were also deemed to have a different competitive dynamic compared to consumer cards with more providers – such as a higher share of three-party card schemes as well as other payment methods such as invoice, direct debit etc.

This is still the case. The EY study notes that commercial cards have a stable and limited market share in the EU (around 3% of transactions), while the average interchange fee for commercial cards remained constant. We believe that the reasons to exempt commercial cards from interchange fee caps in 2015 remain just as valid in 2020, while National Competent Authorities continue monitoring correct application of IFR rules, such as the definition of commercial cards.

Other fees within the 4-party scheme model

We agree with the study's conclusion that there is no need to regulate other fees within the 4-party card scheme model.

In addition to interchange, the EY/CE study also looks at other fees within the 4-party card scheme model such as Merchant Service Charge (MSC) and network/scheme fees. The study does not recommend any further regulation for MSC and network/scheme fees but notes there may be merit in further investigating the structure, transparency and perceived increases of these fees.

In relation to MSC, the study recommends to 'strengthen the provision of transparent, simple, and unblended price information for merchants and investigating further the implied lack of competition'. However, in our members' experience, blended pricing is often favoured by certain retailers (especially small and medium size retailers) due to the simplicity associated with this type of pricing. For a smaller retailer, it is often more important to have a clear overview of how much they can expect to pay for their card acquiring services rather than a detailed breakdown of the various fees involved. Larger retailers on the other hand often favour unblended pricing. In light of this, we note that the EY/CE study has had a very limited response rate from small and medium size retailers which may have impacted the result and conclusion in relation to MSC transparency and the demand for unblended pricing, especially among smaller retailers.

In relation to network/scheme fees, the EY/CE study notes that potential scheme fee increases do not circumvent the interchange caps. Payments Europe agrees that scheme fees and interchange fees are not comparable, and it cannot be argued that scheme fee increases constitute a circumvention of the caps. However, the study also states that scheme fees for international card schemes have risen since the IFR was introduced in comparison to domestic schemes. In relation to this, it is important to note that a comparison of domestic and international card schemes cannot solely be undertaken on a cost basis. International schemes offer superior functionality, with domestic schemes often being followers rather than leaders in key areas such as functionality, security, convenience and innovation. For example, domestic schemes may not offer zero liability fraud guarantees and chargeback options to their cardholders. Furthermore, international schemes have invested significantly in cross-border technology, which is expensive to develop and maintain but highly valued by cardholders. Payments Europe also notes that EY/CE were only able to collate limited data from domestic schemes and it is questionable if the data-sets are comparable. In relation to scheme fee increases, Payments Europe's own evidence suggests that international card scheme fee increases on a per-transaction basis have been marginal during the 2015-2020 period.

Consumer choice at POS for co-branded cards

Consumers have not been given an effective choice of payment brand at PoS and online

Accoring to the IFR, the choice of which payment brand to use for co-branded cards should ultimately lie in the hand of the consumer. While a retailer may suggest a particular brand, the consumer should be given the option to overrride the choice of the retailer. However, this part of the IFR is currently not implemented in practice, as it is most often the retailer who decides which payment brand is used. Either the option for the consumer to override the retailer's default choice of payment does not exist or does not work, or where it exists it is so cumbersome and non-transparent that most consumers do not know about it. This is the case both on- and offline.

Payments Europe does not share EY/CE's suggestion that it would be optimal to secure a default brand choice for the retailers, rather than deliver on the IFR's requirement that consumers have final say in the payment method they prefer. If only the retailers make the choice of brand, schemes will have an incentive to compete only on the retailer side, not on the consumer' side, meaning that the incentives for competition between card schemes on the consumer side through benefits directed towards the consumer is lost and the consumer is likely to be worse off.

ABOUT PAYMENTS EUROPE

Payments Europe is an association of global and European card-based payment solutions providers created to strengthen the voice of the industry. Payments Europe's members are active throughout Europe representing card issuers, card acquirers, four-party card schemes and other stakeholders active in the ecosystem that offer card-based payment solutions. Our mission is to promote a better understanding of the complexity of card payments and the inherent value they bring to society. We support a vibrant, innovative, and competitive European payments market, that is based on a balanced regulatory framework and puts consumers and consumer protection at the heart of everything.