Position Paper

The German Association for Information Technology, Telecommunications and New Media (BITKOM) represents more than 2,100 companies in Germany. Its 1,300 direct members generate an annual turnover of more than 140 billion Euros and employ 700,000 people. They include more than 900 small and medium-sized enterprises, over 100 start-ups as well as nearly all global players. BITKOM represents providers of software and IT, telecommunications and Internet services, manufacturers of hardware and consumer electronics, as well as digital media and Internet economy businesses.

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GENERAL REMARKS

Intention of the European Commission towards interchange regulation

Since the payment service directive was adopted in 2007, the international payments market has changed dramatically. The volume of digital payments transactions has risen immensely and new business models around payments have emerged. The overall intention has always been to further harmonize the European payments market. The implementation of SEPA is an important step in achieving standardized processes across the Euro zone and the rest of the EU. However there are still substantial differences in the payment networks across the different countries.

In July 2013, the European Commission published a proposal for the regulation of interchange fees for card-based payments transactions. It focuses on more competition; more choice and transparency for consumers and merchants; more innovation; and more payment security and customer trust are to be supported.

The proposal introduces a maximum interchange fee for cross border card transactions, followed by a national one. Beyond that it intends to limit the current card system regulations. The regulation targets a maximum interchange fee for debit and credit card transactions of 0.2 and 0.3 percent of the transaction amount. In the first phase the regulation will be deployed on all cross border transactions. In the second phase 22 months later, all national transactions will be capped at the same amount.

Economic viability and commercial incentive throughout market dynamics and not further regulations

BITKOM believes that the regulatory framework in the European Union provides an adequate environment for business and innovation in the area of e- and m-commerce, including payments. EU legislation on payments, e-money and consumer rights, among others, is among the most advanced globally, and serves as examples for many countries around the world that want to achieve similar market integration, innovation and prosperity. This holds also for the European payments market.

BITKOM agrees that a competitive environment is conducive to business development and beneficial for end-users and consumers. BITKOM does not conclude, however, that competition is the only factor shaping the payments market. In particular innovation arises from factors and motivations which go beyond or are independent to an extent from the regulatory framework for competition.

BITKOM strongly supports the initiative to foster digital and card payments and to reduce cash payments. This is in the best interest of all stakeholders like commerce, banks, consumers, political bodies, card systems and other digital payments provider. The desired harmonization of the European payments market is the key target of BITKOM and its members. But we believe that commercial rationale is the obvious market dynamic, driven by consumer preference, which will determine economic reward, not regulation.

BITKOM is certain that the regulation is taken an unnecessary intervention in the competitive and dynamic payments market across Europe. There are a rather large number of payment services providers across the EU member states, which provide services either domestically or cross-border. Choice and competition are satisfactory for large or small businesses, as well as for consumers.

BITKOM is convinced that the prospect of economic reward is the key driver for innovation. More competition therefore will not in itself lead to more innovation, or to improvements for the consumer as regards payments. Neither will regulatory efforts to enhance competition, or to achieve other objectives, automatically deliver innovation. Instead, it is of fundamental importance to follow a more general economic, commercial rationale, and approach competitive and other regulatory considerations from this angle.

Some examples may highlight the significance of this perspective. Interchange, as a principle, follows warranted commercial considerations. Choice and the availability of different products may be smaller in some markets than in others, if consumers do not derive additional benefit from additional choice.

BITKOM supports the Commission’s commitment to providing a competitive environment for market growth, and confirms the Commission’s prime responsibility in preventing market abuse and anti-competitive tendencies. BITKOM however cautions that the regulation will have rather negative consequences for the consumer. Measures proposed in the draft legislation will not help in the achievement of these objectives. To the contrary, there is clear empirical evidence that many of the proposed measures will in fact go against the market harmonisation, fair competition, consumer protection and merchant interests that the European Commission claims to be seeking to promote.

The pace of development in payments innovation has increased significantly with the development and increasing prevalence of the internet and more recently multi-functional mobile phones. The evolution is still ongoing and any final scenario cannot be predicted. This creates obvious challenges for the European Commission and other legislators, as market growth and innovation needs a conducive regulatory environment, but consumers and businesses also need to be protected from potential new risks.

Regulatory neutrality must be respected as regards the various types of payment systems and methods. While some methods may be perceived as more prevalent than others, BITKOM points out that payment preferences vary from country to country or even from one transaction type to another. These preferences cannot be changed by prescriptive regulatory attempts. If at all, long-term education and pragmatic use cases may shift users ‘payment preferences in an overall market-driven process.

BITKOM reiterates that economic reward is a necessary and sufficient condition for innovation, and the most reliable driver in the current market evolution towards new dimensions for businesses and consumers. BITKOM therefore insists that any regulatory interference deemed necessary must not disrespect regulatory neutrality.

Interchange Fees – Chapter II, Article 3 & 4

Interchange fees for consumer debit and consumer credit transactions in the EEA will be capped at 0.2 and 0.3 percent of the transaction value. These caps will enter into force in a staged approach:

- In the first stage, all cross-border transactions in the EEA Member States will have to comply with the caps. But the caps would also apply to centrally acquired (domestic) transactions, i.e. when a merchant contracts with an acquirer established in another EEA Member State, that (central) acquirer will pay maximum 0.2%/0.3% interchange fee.
- In the second stage, 22 months later, all transactions – including domestic transactions acquired by a domestic acquirer – would be capped at the same levels.

Commercial card interchange fees are not subject to the cap (but are subject to the other provisions of the proposed Regulation).

All forms of interchange fee setting would be covered, i.e. when set by the scheme, or set multilaterally by the banks, as well as set bilaterally by an issuer-acquirer pair.

RESPONSES:

- As the stage of development of card payments varies considerably between Member States, the interchange fees differ significantly as well, thus allowing for the flexibility necessary to ensure vibrant and innovative card payments.
- Interchange caps of 0.2% and 0.3% are levels arbitrarily defined by the EC, without any sound methodology or any data to support them:
    - The Commission claims that the levels are based on the Merchant Indifferent Test (MIT). The fundamental premise underpinning the MIT is that merchants do not receive more benefits from a card payment than from a cash payment; therefore the cost for the merchant of accepting a card payment or a cash payment should be the same. However the MIT is not an appropriate methodology for setting the level of interchange fees.
    - The economic literature does not suggest that the MIT is an appropriate means to assess benefits resulting from interchange fees the MIF for the purpose of the application of competition law. Rather than assessing “efficiencies” as required under Art. 101(3) TFEU, the MIT aims at removing any impact on the merchant that arises from the consumer’s customer’s choice of payment method.

  - Merchants receive numerous benefits from card payments that they do not receive from cash – and therefore cash is not a proper comparator for cards. For physical merchants, credit cards, for example, offer a credit facility which allows consumers to make a purchase now rather than later, but also to spend more at the merchant (incremental spend). For online merchants, cash-on-delivery is most often no an attractive or practical option and therefore the benefit of cards over cash is obvious.
  - In addition, in order to support the MIT, the EC has commissioned several studies. The first one, performed by EIM, seems to be completed – however the EC has always refused to reveal its content. Other studies, entrusted to Deloitte Consulting, are still on going and, therefore, cannot provide any justification for 0.2 / 0.3%. Curiously, they are not even referred to by the Commission in the proposed Regulation.
- Setting artificial, inflexible interchange caps is tantamount to “price” regulation, which should always remain a “last resort” measure as it runs directly contrary to the principles of free competition and the fundamental objectives of the EU Treaties.
- The impossibility for an issuer and an acquirer to agree on a bilateral level of interchange different from that proposed in the Regulation goes against the fundamental principle of contractual freedom that parties should have to enter, or not, into a commercial agreement.
- Despite the statements made by the Commission about the alleged lack of competition, the payments market is highly competitive and does not prevent new players from entering the market. There are numerous new companies that have successfully entered the vibrant and fast evolving payments market.
- More immediate negative consequences of the proposed Regulation would include: increased cardholder fees; increased cost of accepting cards for SMEs; impediment to the healthy development of card payments (e.g. contactless payments, mobile payments, digital wallets, etc):
  - Past experiences in Spain, Australia and more recently in the US demonstrate that a coerced reduction of interchange will lead to an increase in cardholder fees, thus making cards more expensive for consumers. It will also lead to a reduction in the benefits granted by issuers to cardholders, along with the reduced availability of credit for consumers and SMEs.
  - As a result, consumers will be less inclined to use electronic payments and therefore use more cash instead, increasing the shadow economy and reducing Member State’s income from taxation. This will also reduce the benefits that merchants get from card payments.
  - The experience in Spain, Australia and the US also shows that the reduction in the cost of accepting cards that large merchants will benefit from will not be passed onto consumers.

SUGGESTION:

BITKOM would like to suggest eliminating article 4, because an artificial interchange at one rate for all nations cannot reflect the different competitive payment environments within the countries. Today you have different players in the markets that set their fee in accordance to the market situation. The artificial "one fee fits all countries" scheme would therefore harm competition and would be contradictory to its overall target – promoting digital payments, competition and positive spill over for consumers.

Level Playing Field – Chapter II, Article 5

The scope of the proposed legislation covers all four party card schemes (MasterCard, Visa and domestic schemes in some EEA Member States) as well as three party card schemes (which offer issuing, acquiring, scheme, as well as processing services to cardholders and merchants), with however two majors exceptions: (1) the interchange fee cap and (2) the separation of scheme and processing. Those two majors provisions of the proposed legislation will not apply to three party card schemes, such as American Express (Amex), except when the scheme "licenses other payment service providers for the issuance and/or the acquiring of payment cards" (Article 2(15)), such as in the Amex GNS model.

RESPONSES:

- In order to provide a true level playing-field, it is essential that also 'pure three party card scheme' transactions (e.g. Amex proprietary, Diner's) are covered by the interchange cap.

- In its resolution of 20 November 2010 on the EC's Green Paper, the European Parliament was very clear on the issue of level playing field: it clearly called upon the Commission to propose legislation that would cover all card payment schemes, irrespective of their business model (four party schemes, mixed schemes or three party schemes), otherwise the proposal would discriminate four party against three party schemes, and lead to a deep competition bias in favor of the latter.

SUGGESTION:

BITKOM suggests that if regulation occurs, it is important that it includes all relevant schemes, which means that three party schemes have to be taken into consideration in all aspects of the regulation as well, not only four party schemes.

Honour All Cards Rule – Chapter III, Article 10

The European Commission proposes that the 'Honour All Cards rule' (HACR) be relaxed so that merchants cannot be required to accept two products belonging to the same brand and/or category (e.g. debit, credit, prepaid, commercial), unless these two products are subject to the same regulated interchange. The most obvious consequence of this relaxation is that a merchant may decide to accept only consumer cards (subject to an interchange fee cap) but not commercial cards (not subject to an interchange fee cap).

In order to allow merchants to exercise their right to refuse certain brands / categories, issuers will be required to label the cards so that the brands / categories (i.e. prepaid, debit, credit or commercial) are visibly and electronically identifiable to the merchant.

RESPONSES:

The HACR is vital to any payment scheme and the proposed relaxation would create uncertainty for consumers and merchants:

- Merchants are free to choose whether or not to accept payment cards. Once a merchant has decided to accept payments cards, the merchant is free to decide which brands he would like to accept. Merchant can usually decide whether he wants to accept only debit cards or only credit cards or both.
- Competition is fierce between issuers, acquirers and payment schemes. Payment schemes compete across various product categories (e.g. debit / credit) and across various segments (e.g. consumer standard or consumer premium). Eliminating the HACR will not drive competition faster than is already the case.
- However, eliminating the HACR would be a very anti-consumer measure: It will create confusion and uncertainty for the cardholder.
    - The HACR is a requirement in any payment scheme – in particular for an international payment scheme involving tens of thousands of banks around the globe. The consumer is attracted to such products in the first place because of the promise of a universally accepted, hassle-free payment method.
    - Eliminating the HACR would limit card acceptance for consumers (i.e. certain customers would see their card being declined and may not have another means of payment immediately available). This ultimately would limit international use (tourists and corporate expenditures).
    - This would also impact the merchant in the form of lost sale opportunities.
- If the cardholder has no guarantee that his card will be accepted, the card is worthless to the cardholder. Cash usage may consequently be stimulated, along with all the associated societal costs.
- Eliminating the HACR would slow down innovation:
    - Thanks to the existing HACR, schemes leverage the value of their brand in order to introduce new products to the market.
    - If the possibility of requiring the merchant to accept different types of cards under the same brand was suppressed, it would become increasingly difficult for schemes to develop new products and innovate, as they would have no guarantee that the investments could be recouped through the acceptance and use of the products.

If HACR is relaxed, BITKOM believes this would negatively hurt the consumer, merchants and innovations. As regards unregulated cards (e.g. commercial cards), under the proposed Payment Services Directive 2 (PSD2), merchants will be able to surcharge those cards if they wish to do so. In addition, merchants are free to steer the consumer towards their preferred means of payments through methods other than surcharging – e.g. by offering a discount for cash payments if they so wish. This means that the merchant is more than sufficiently equipped to steer the consumer away from products that it would consider as being “too expensive”.

SUGGESTION:

BITKOM suggests that the honor all cards rule should still be applied and that the merchant will not need the power to refuse or surcharge any commercial cards.