

19 SEPTEMBER 2014

## EPIF POSITION ON THE DRAFT REGULATION ON INTERCHANGE FEES FOR CARD-BASED PAYMENT TRANSACTIONS

---

### ABOUT EPIF (EUROPEAN PAYMENT INSTITUTIONS FEDERATION)

---

EPIF, founded in 2011, represents the interests of the non-bank payment sector at the European level. We currently have over 170 authorised payment institutions and other non-bank payment providers as our members offering services in every part of Europe. EPIF thus represents roughly one third of all authorized Payment Institutions in Europe.<sup>[1]</sup> Our diverse membership includes the broad range of business models including:

- 3-party Card Network Schemes
- Acquirers
- Money Transfer Operators
- FX Payment Providers
- Mobile Payments
- Payment Processing Service Providers
- Card Issuers
- Third Party Providers
- Digital Wallets

EPIF seeks to represent the voice of the PI industry and the non-bank payment sector with EU institutions, policy-makers and stakeholders. We aim to play a constructive role in shaping and developing market conditions for payments in a modern and constantly evolving environment. It is our desire to promote a single EU payments market via the removal of excessive regulatory obstacles.

We wish to be seen as a provider for efficient payments in that single market and it is our aim to increase payment product diversification and innovation tailored to the needs of payment users (e.g. via mobile and internet).

EPIF is glad to share its position on the draft Interchange Fees (IF) Regulation with the EU policymakers.

---

<sup>[1]</sup> According to the Eur. Commission, there were 568 authorized Payment Institutions in Europe as per end 2012.

## 1. INTERCHANGE FEES

---

The basis for the Commission’s proposed action in this area is the antitrust concerns related to the fact that merchants typically have no choice but to accept inter-bank network cards such as Visa and MasterCard and the interchange fees that accompany them.

Smaller, non-bank networks, including those that work with select partners on a bilateral basis, should not be included in the scope of any IF regulation, as they do not have interchange fees nor do they have the characteristics of dominance or collective practices that are a feature of four-party schemes, which have been the subject of multiple competition law investigations in the EU.

EPIF is concerned that the previous critical interventions by the Commission that have enabled “three party” schemes to effectively compete will be undermined by the draft legislation. For example, the Commission intervened in 2007 to ensure non-bank schemes with bilateral licensing arrangements retain flexibility to select their partners via a carve-out from “open access” requirements in Article 28 of the PSD; and more recently, to ensure the representation of payment institutions in the European Payments Council.

Regulating the licensing relationships in “three party” schemes now would therefore mark a significant departure from existing legal and regulatory precedents, which specifically recognise the unique business model and structure of these schemes, including where licensing partnerships are involved.

Regulation should not be forced on players to whom the above-mentioned competition concerns do not apply. There is no justification for placing limits on the flexibility of smaller schemes to negotiate pricing with their licensing partners. Any such attempt would eliminate an important point of differentiation that smaller, non-bank schemes can offer their partners and, in turn, end customers. It would dramatically undermine the economic viability of those partnerships and, with it, the ability of smaller, non-bank networks to act as a counterweight to the dominant, inter-bank schemes.

The policy implications of applying interchange caps to such partnership arrangements are alarming, since the caps would then extend well beyond collectively-set and mandated fees (as in the inter-bank schemes) and also catch fees freely agreed between two commercial parties negotiating at arm’s length.

We believe the EU should take action to protect and foster competition and innovation in payments, by ensuring that smaller, non-bank networks retain the commercial flexibility needed to negotiate arrangements that allow them to compete effectively with the dominant, inter-bank networks.

We also warn against any attempt to assimilate **digital wallets** to card schemes<sup>1</sup>. The goal of the proposed Regulation is to lay down uniform technical and business requirements for payment card transactions carried out within the EU. Thus, the focus of the Regulation is exclusively related to card scheme payments. Any inclusion of digital wallets in the Regulation is misleading and risks distorting the aim and scope of the Commission's proposal for the following reasons:

- Digital wallets typically allow users to pay using their card, but also through alternative funding instruments, such as their bank account or their account balance. Imposing price caps on digital wallets would then have the unintended effect of **exceeding the objective of the Regulation, which is aimed at card payments only**;
- Digital wallet providers are not card schemes. They are not a bank acquirer and do not issue cards. On the contrary, **digital wallets providers are users of card schemes and pay interchange fees to four-party scheme acquiring banks. The fees charged by digital wallets to their customers are not interchange fees.** It is meant to compensate digital wallets for the provision of a service allowing customers to pay using their payment card, their bank account or their account balance.
- As per the Commission's proposal, the purpose of the Regulation is to eliminate the anti-competitive impact of multilateral interchange fees in four-party card-based payment transactions. **Digital wallets are neither card-based transactions, nor have they been singled out by the Commission as having an anti-competitive impact.** Multilateral interchange fees pertain to four-party card schemes only, while digital wallets and other Payment Service Providers (PSPs) only have merchant fees.

EPIF therefore urges policymakers to make clear that three-party schemes with licensees and digital wallets are not within the scope of the pricing caps in the IF Regulation.

EPIF's acquiring members that work with four-party card schemes also request that there is an adequate and reasonable notice period for implementation of the regulation in order to accommodate necessary complex system and hardware changes. These impacts are likely to be most pronounced in the implementation of the unblending, Honour-all-Cards, co-badging and separation of processing provisions that, depending how finalised and interpreted, could imply major changes to complex billing, authorisation and clearing systems and/or acceptance hardware.

---

<sup>1</sup> It is important to clearly differentiate digital wallets - provided by companies such as PayPal - from virtual wallets provided by four-party card schemes: in fact digital wallet providers are not necessarily card schemes.

## 2. PAN-EU LICENSING

---

One of the requirements of the draft proposals is that all issuers and acquirers for any network – including “three party” schemes with licensees – must be permitted by card networks to offer their services throughout the EU on the basis of a single license from the network.

This requirement is directed at arrangements that restrict the ability of parties to operate in specific geographic areas, which in some circumstances could serve to segment the market and can work against the achievement of single market objectives.

At the same time however, it is important to acknowledge that in some circumstances territorial restrictions can *promote* inter-network competition and the ability of smaller networks to grow relevance and coverage on a pan-European scale. This is particularly important where the network’s sector share is small, and every investment made by a licensee in that network plays a critical part in supporting the growth of the network and thereby enhancing competition with larger networks. Without the ability to provide exclusivity, smaller networks would be inherently handicapped in their ability to grow relevance and coverage across Europe, to the benefit of the dominant, inter-bank networks.

This is the case with EPIF’s three-party network members. The pan-European licensing requirement would cause fundamental damage to those partnership business models and disincentivise partners from investing in that network in a given country. Ultimately, it could force them to discontinue business in some countries. In turn, this would lead to less choice for consumers and merchants and would only reinforce the dominance of the incumbent “four party” schemes.

EPIF urges policymakers to maintain this balance by exempting “three party” network licensing arrangements from the scope of the pan-European licensing requirements in the proposals.

## 3. SEPARATION OF PAYMENT SCHEME AND PROCESSING ENTITIES

---

Although the draft proposals currently exempt “three party card payment systems” from these requirements, the definition of this term would still appear to subject “three party” networks to these requirements in cases where they operate with licensing arrangements for issuing or acquiring.

These draft proposals assume incorrectly that all card schemes operate on the basis of inter-bank relationships and enjoy a dominant market position. Furthermore, at a practical level, it is not clear how the separation requirement could apply in view of the structure of three party card scheme’s licensing arrangements, in which there are no inter-bank arrangements to be processed and therefore none to be separated.

This was recognised by the European Central Bank in its 6<sup>th</sup> SEPA Progress Report in 2008, and incorporated by the European Payments Council in v2.1 of the SEPA Cards Framework, both of which

exempt “three party” schemes, including those with licensees, from requirements to “unbundle” processing from scheme management.

EPIF urges policymakers not to apply requirements around separation of processing to “three party” networks, including those with licensees.

#### 4. “HONOUR-ALL-CARDS” RULE

---

The “Honour All Cards” requirement is based on the principle that a card network must be able to give cardholders certainty as to where their network-branded products will be accepted. This is most effectively achieved by requiring merchants to accept all cards of the network and display the network’s acceptance brand.

When merchants display a card network logo – be it Visa, MasterCard, American Express or Diners Club – they are representing to consumers that the cards of the brands displayed will be acceptable forms of payment without being inconvenienced by a merchant’s selective rejection of those cards or a request to use another payment method.

Given that EPIF’s three-party scheme members do not have market power, merchants have a clear and free choice as to whether or not they accept their cards. It is essential to expect that once a merchant makes the choice to accept one card from such a scheme, it will honour this basic commitment to all cardholders of that scheme.

In addition, the pricing that three-party schemes typically agree with their merchants is simple and transparent: merchants agree a single rate for every card transaction, regardless of the card type. In contrast, on most inter-bank networks, merchants are faced with a dizzying array of rates, reflecting in part a range of product- and segment-specific interchange fees agreed upstream among the member banks. As such, the price differences which could lead to a desire for selective acceptance among same type card products bearing the same brand in the dominant card networks are not present for three-party scheme cards.

Like so many other issues covered in the draft proposals, the notion of allowing merchants to accept or reject particular cards within a network arose from antitrust concerns related to multilateral interchange fees. These are not concerns that apply to smaller, non-bank networks, and there is therefore no justification to prohibit the “Honour All Cards” provisions in the agreements of merchants who choose to accept cards from these networks.

More generally, selective card acceptance would be cumbersome for merchants to implement and even more so for their customers to understand. Merchants’ employees would have great difficulty, for example, differentiating among cards displaying the same card network logo. This kind of complexity is highly susceptible to mistakes or abuse.

EPIF urges policymakers to continue to permit “Honour All Cards” requirements in Europe.

## 5. STEERING

---

Proposals to prohibit anti-steering rules rules to allow merchants to promote preferred payment methods, arose in antitrust case related to interchange. As is clear from the issuing share figures cited by the Commission, unlike Visa and MasterCard, EPIF’s three party scheme members do not have market power. Merchants have a clear choice whether or not to accept their cards, a fact which is underscored by their lack of universal acceptance among merchants.

There is therefore no justification to prohibit the “anti-steering” provisions in card acceptance agreements with merchants who choose to accept cards from three party networks.

It is very difficult for merchants to steer Visa or MasterCard cardholders to smaller three party card schemes because most consumers do not carry those cards. By contrast, it is very easy for merchants to steer cardholders of smaller three-party card schemes toward using Visa and MasterCard, given the ubiquity of those schemes’ cards – the net result being more business for the two dominant networks.

The ability to agree an “anti-steering” requirement with merchants is part of the commercial flexibility that smaller networks need to maintain positive point-of-sale experiences that meet their cardholders’ expectations and enable these schemes to compete more effectively with the dominant, inter-bank networks.

EPIF urges policymakers not to introduce steering tools for merchants .

## CONCLUSION

---

Finally, EPIF welcomes the opportunity to engage further with relevant EU Institutions on the issues highlighted above. EPIF would be happy to provide any technical input or any other helpful information, including the substantiation of the points made above or with regards to explaining how the proposals apply to the different business models we represent.

For more information about the PI sector, the EPIF organisation and its members or our position papers, please contact us via our website or Secretariat.

