European Commission

The interchange fees regulation

What is it about?

Payment cards are one of the most important means of retail payments, especially for cross-border and internet purchases. Payments are estimated by the ECB[1] to represent a total cost to society of about 1% of GDP or EUR 130 billion per year. Revenue from payments is estimated at about 25% of total bank revenue in the EU [2] .Whereas in some countries payment card transactions still represent a small share of point of sale retail transactions (Italy 7%, Romania and Greece 2%) [3], in other countries this goes up to 66% (Netherlands), 69% (UK) and 72% (Sweden)[4].

Interchange fees are paid by the retailer's bank to the cardholder's bank for every individual transaction. Fees vary depending on the type of card: For a payment transaction of EUR 100, around 6 cents would typically be paid in a scheme like Bancontact in Belgium, 3 cents to EUR 1.50 for an international debit card (e.g. Maestro/ V-Pay), EUR 0,70 to EUR 1.50 for a credit card (e.g. MasterCard/ Visa), up to EUR 1.90 for a premium or commercial card, and EUR 2-3 for an AMEX card.

Fairness

Through their bank, retailers pay the interchange fee each time a customer uses a payment card – EUR 9 billion annually in interchange fees alone. They have **no choice**: if they don't accept card payments they risk losing customers, and they can't negotiate the fees as these are fixed jointly by the banks or by the card schemes on their behalf. In the end, consumers pick up the bill in the form of higher retail prices. Card issuing banks use reward schemes to incentivise consumers to pay with the cards providing the highest fees to the bank. In fact, the 'poorer' customer who pays with a debit card or in cash pays for the air-miles given to the 'richer' customer who is provided by his bank with a –higher fee- credit card or Amex card.

The Commission wants interchange fees to be both **fair and transparent**. Today, they are often unfairly high and opaque. The Commission also thinks that retailers should be able to freely choose the cards they accept.

Protecting the Single Market for the benefit of consumers

A well-functioning payment system is essential for the single market. Interchange fees are a barrier to this. Today, the EU is **artificially sliced up** into 28 national markets with wildly diverging fees – from less than 0.1% in some Member States to more than 1.5% in others – and retailers are prevented from receiving better prices available in other countries. **This is a direct attack on the single market.**

In the Commission's **antitrust cases**, MasterCard [5] and Visa [6] have offered to cap their cross-border interchange fees at 0.2% for debit cards and 0.3% for credit cards. National Competition Authorities (NCAs) are also looking at interchange fees. These cases lead to a patchwork of solutions addressed to individual payment schemes, and are unlikely to provide a level playing field soon. The absence of regulation in this area facilitates market fragmentation by payment card schemes and banks.

Regulating interchange fees will **benefit consumers and retailers** - particularly in Member States where current fees are very high. We do not expect a significant effect on card holder fees, because these are set competitively by issuing banks. In fact, card holder fees seem to reflect the level of competition in retail banking in each Member State, so where other bank fees are high, card holder fees are high. Card holder fees are relatively transparent and so if they are too high consumers can move banks. This, for example, happened in the US where banks threatened to increase card holder fees when their debit MIFs were capped. But card holders threatened to switch banks and so the increase was withdrawn.

Enabling newcomers to give retailers and consumers a better deal

The current fragmentation of the European market also prevents new players from offering better and cheaper EU-wide solutions. Such **solutions** typically entail a single interchange fee across the EU – while banks expect to receive fees at least as high as the ones prevailing in a given Member State.

Creating a **level playing field** through Regulation will facilitate market entry of new players.

Spurring innovation

Payments via **mobile phones** are increasing, and in the future we may see many different means of payment 'co-badged' on our mobile phones (e.g. debit card, credit card, credit transfer). Undistorted competition will lead to **innovation**. However, the problems in the card markets today are already spilling over into the new markets of internet and mobile payments. This is why we need to **act now.**

Incidentally, there is no evidence that high interchange fees would lead to more innovation. Most payment schemes in the EU were established before the current levels of interchange fees. And many investments in innovative payments (e.g. terminals for mobile payments), are made on the acceptance side by banks and retailers that *pay* the interchange fees - not by those that *receive* them.

Inverse competition leads to higher prices for consumers and retailers

Market mechanisms in the payments market drive prices up rather than down. Competition takes place on the issuing side; card schemes have an incentive to offer higher interchange fees to banks to have their cards issued.

On the other hand, **retailers cannot defend themselves** against increasing fees. In practice they are compelled to accept the main consumer card brands. The UK offers a good example of this, with the national card system Switch being replaced by Maestro and then Visa Debit - each time with *higher* fees. Interchange fees have doubled from 4 pence to 8 pence per transaction between 2005 and 2007, and almost all retailers still feel obliged to accept them.

Main elements of the proposed regulation[7]

Imposing caps for interchange fees for the most frequently used cards.

The proposed cap is **0.2% and 0.3%** per transaction for consumer debit and credit cards, respectively. In the framework of **competition commitments,** Visa Europe, MasterCard and *Groupement des Cartes Bancaires* have already accepted equivalent caps. Fees at these levels have been in place since 2009 in some cases and they have not threatened anyone's viability. **These caps must apply per transaction and not on the basis [8]of a weighted average.** Only then will retailers be able to check and challenge the fees they pay – which at the same time would limit the need for detailed and difficult monitoring of the regulations by public authorities.

The caps on interchange fees would apply to **cross-border transactions in a first stage,** including when merchants use an acquirer outside their own Member State.

This is a key provision that prevents the card schemes from **slicing up** the single market into separate national markets. Under the commitments offered by the two international schemes the reduced fees already apply when consumers use their cards abroad. However, as proposed by the Regulation, they should also apply when retailers chose to use card acquiring services offered by banks in other EU Member States. This is the **single market at work**. The Commission is pursuing this segmentation against Visa and MasterCard because it restricts competition. Visa Europe has proposed to remove the market fragmenting rules in its commitments published in 2013, scheduled to enter into force in January 2015.

The interchange caps will be extended to domestic transactions after two years.

This will ensure that **all merchants** – and as a consequence consumers – can benefit, and it will create a genuine single market in payments.

Introduce more transparency and effective competition.

It is not necessary to also regulate fees for cards that are less widespread. However, in that case retailers should no longer be obliged by the schemes to accept such non-regulated, higher fee cards. They should also be able to surcharge consumers for the use of such cards, avoiding that others pay for the individual cardholder's benefits. In order to allow such market forces to work, retailers and consumers must have **more information** about the cost structures and interchange fees, including through the identification of the individual (card-based) payment instrument. This will enable them to make informed choices through greater competition.

In the near future consumers will be able to pay with a variety of payment instruments and brands on one **mobile phone**. It is important to leave the **choice** of the instrument to those who will bear its costs, i.e. retailers and consumers.
Payment card schemes, banks and wallet providers should therefore be prohibited from programming the order of priority of payment applications in cards, mobile and terminals to select the most expensive brand for the payment.

The proposal builds on 20 years of experience in competition cases.

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[1] ECB Occasional Paper Series, No. 137, Sept. 2012.
[2] ECB at "The future of retail payments: opportunities and challenges" Vienna, 12 May 2011.
[3] ECB Occasional Paper Series, No. 137, Sept. 2012, figures in volume of transactions.
4 DNB Occasional Studies Vol. 11 Nr 2 (2013), BRC Cost of Payment Collection survey 2012 and Sveriges Riksbank Working paper series 262 (2009 data). Figures in value of transactions.
[5] http://europa.eu/rapid/press-release_IP-13-314_en.htm?locale=en
[6] http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=1_39398
[7] http://ec.europa.eu/competition/sectors/financial_services/payments_en.html