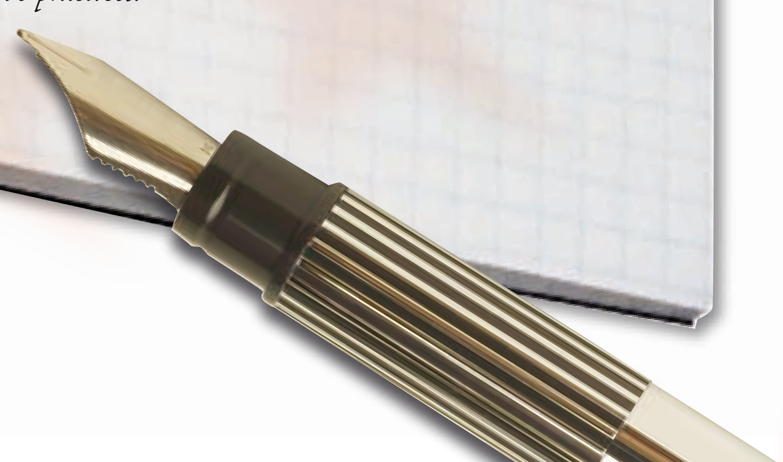
A real single market for payments and SEPA are highly desirable

Every European consumer would benefit from a more competitive single market for payments through lower prices and increased choice. To achieve this:

- ✓ *The Payment Services Directive must be implemented by Member States as soon as possible and lead to greater transparency (notably in card fees), efficiency (by increasing competition at all levels of the payment value-chain), and the emergence of new payment systems providers (non-banks and private labels).*
- ✓ *SEPA should lead to lower cost payment systems; huge economies of scale should, as in any other business, lead to lower prices.*
- ✓ *The level of competition should increase and anti-competitive practices by card schemes should be banned. Competition authorities should continue to watch over the sector.*
- ✓ *Retailers and consumers should be entitled to more transparency with regard to their bank fees.*
- ✓ *Retailers should not be forced to pay for services from which they do not benefit.*

What SEPA for cards should mean

1. *Price of card payment instruments should decrease;*
2. *Efficiency of payment instruments should not be sacrificed;*
3. *Retailers should be able to buy their services anywhere in the EU ... as with any service;*
4. *There should be more, not less, competition between services providers at all levels of the value-chain, and there should be more providers including non-banks and private labels;*
5. *Retailers should be allowed to buy and negotiate the services they desire, and only those;*
6. *Retailers should be allowed to tell their customers that some payment instruments are more expensive than others in order to allow the customer to make an informed decision;*
7. *Increased competition will deliver a more vibrant and innovative payment cards market in which products succeed because they serve the interests of the customers, not because they are protected by anti-competitive practices.*



EuroCommerce

THE RETAIL, WHOLESALE AND INTERNATIONAL TRADE REPRESENTATION TO THE EU

Printed June 2007 www.inextremis.be

Commerce is the closest link between industry and the 493 million consumers across Europe. It is also the largest consumer-related market service. It is a dynamic and labour-intensive sector, which plays a significant role in the European economy, generating 11% of the EU's GDP through 6 million companies. Over 95% of these are small enterprises that are vital to Europe's economic and employment prospects. The sector is a major source of employment creation, providing jobs for 30 million people from all parts of society and is one of the few economic sectors generating increased employment.

EuroCommerce
Avenue des Nerviens 9-31
B- 1040 Brussels

Tel: +32 2 737 05 98
Fax: +32 2 230 00 78
E-mail: bastings@eurocommerce.be
www.eurocommerce.be
www.StopUnfairCardFees.eu

Printed on elemental chlorine free paper.

EuroCommerce

MAKING PAYMENTS WORK IN EUROPE

Europe is slowly heading towards a Single Market for Payments

The logical follow-up to the introduction of the euro was to create a real single area for payments, in which all European consumers would be able to pay abroad as easily and as efficiently as in their home country.

The European Union made huge progress by adopting Regulation 2560 on cross-border payments in 2002 and the Payment Services Directive in 2007. At the same time, increasing political pressure pushed the banks to standardise infrastructures in the euro-zone by 2008, in order to realise SEPA (Single Euro Payments Area). Europe now needs to make sure that this great idea on paper will facilitate the introduction of more efficient and less expensive payment systems in practice.

Many problems remain

The Commission sector inquiry on retail banking has underlined that major problems still exist in the field of payment systems: distortion of competition, lack of transparency and substantial entry barriers, in particular in the card payment market. Some of these barriers may result from abuse of a dominant position or from co-ordinated behaviour of incumbents to exclude newcomers.

The report also underlines the enormous profitability of some banking activities: in 2004, the profit-to-cost ratio of card issuing was 65% and that of card acquiring 47%.

Consumers pay an exorbitant (hidden) price for payment services

We are all consumers of payment services, but their costs are well hidden: banks issuing cards charge retailers, via their acquiring bank, a percentage of each transaction. This is called the interchange fee. It is not negotiable and often accounts for more than 80% of the fee a merchant pays to his bank.

The heart of the problem lies in the way the costs (and the profits) are distributed amongst the different participants in the transaction: most of the costs of card payment systems are borne by retailers through the interchange fee. Yet these fees cover services and "gifts" that are promoted by banks to entice more card users to choose their particular brand. These services and gifts include interest-free period, air-miles, cardholder insurance, promotional campaigns selling these gifts and so on. The interchange fee also covers fraud arising from the banks' own poorly developed products.

Therefore, when consumers pay with Visa or MasterCard, they are not aware that this simple act results in a significant cost for the retailer.

Retailers have no other choice but to add the fees for accepting cards to the price of goods, which all customers pay, regardless of whether cash or a card is used.

So, should retailers really have to subsidise the banks' profits and pay for services from which they do not benefit?

In effect, payment systems cost:
- €139 per year per household[1], whether they pay by card or not
- €25 billion for business in card fees[2], of which the interchange fee accounts for a significant part.

The interchange fee is a huge source of unfair profit for banks

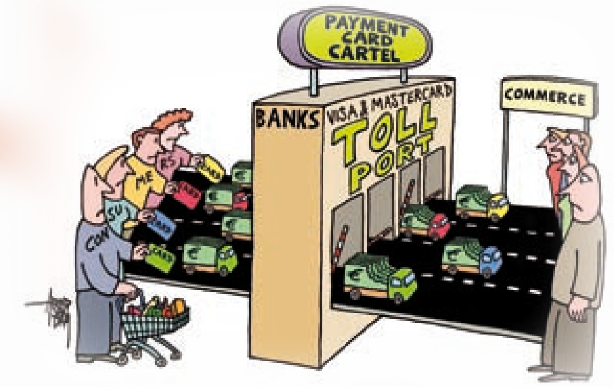
The sector inquiry revealed that, if the interchange fee increases by €1, only 25 cents are passed on to the cardholder in lower fees; the banks retain 75 cents as profit! The inquiry also found that issuing activities would remain profitable without interchange fees in 21 EU Member States.

The system is unfair...

Unfair for consumers: through higher prices for the products they buy and cross-subsidisation of costs because consumers who do not use cards pay for the "gifts" given to those who do!

Unfair for retailers: small retailers (i.e. 95% of retailers) pay substantially more for card acceptance than larger ones. Even large retailers have very little negotiating power with their banks over the fees they pay; the interchange fee is not a negotiable part of their contract. But many retailers are practically obliged to accept cards ... because consumers like cards!

... not transparent,



Most retailers receive no information about card fees, and furthermore, card schemes forbid retailers from informing their customers about card fees. Consequently, consumers do not know that the costs of all goods are inflated because some use expensive means of payments.

... and inefficient

There is a cross-subsidisation between payment means, resulting in the replacement of efficient means by less efficient ones.[3] Moreover, the system carries no incentive for banks to even try to reduce fraud, as it is paid by third parties, i.e. retailers and their customers.

SEPA should mean good news for consumers

EuroCommerce is very supportive of the whole SEPA concept as part of the opening of the Internal Market process and standardising infrastructures. Unfortunately, despite the good intentions of the European institutions, turning this concept into reality could act as a Trojan horse carrying a major threat for retailers and consumers. This threat is created by replacing efficient and cheap national debit card schemes with the more expensive interchange fee-based Maestro and V Pay (the debit schemes of MasterCard and Visa). Retailers in the UK and Switzerland went through the painful experience of this replacement; their bank fees increased by up to 400%!

Facing the tough deadlines imposed by the SEPA framework, banks have two alternatives: make the low-cost, efficient national debit card schemes work on a pan-euro-zone basis or move to Visa and MasterCard's ready-made solutions. Considering that Maestro and V Pay are interchange-based and therefore more lucrative for banks, it is therefore clear that banks will opt for the more profitable but less efficient option to the detriment of retailers, consumers and the wider economy.

As Neelie Kroes[4], European Competition Commissioner, said, "the costs of high interchange fees are of course being passed on to all customers through higher retail prices". The increasing dominance of Maestro and V Pay implies that the costs of all retail goods are likely to increase, to the detriment of all European consumers.

1 Assumed size of household: 2.5 people. Total cardholder fees = average of annual card fee figures (Sector Inquiry) x stated number of cards in Europe (145 million for MasterCard – MasterCard press release, 01.11.06; 300 million for Visa – Visa website, 'Statistics')
2 Neelie Kroes, SPEECH/07/186, 26 March 2007

3 Gresham's law of payments
4 Neelie Kroes, "Getting more from financial services markets: greater competition for a better deal for consumers", The Future of Europe, public lecture series, London School of Economics, London, 19 February 2007