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Interchange fees, Fear or Confidence ?



PaySys

Friday 23rd April 2004 - Frankfurt

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Interchange fees, between fear and confidence

I. Factual background

II. Multilateral interchange fees (MIFs) and EU competition law

III. The way forward



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I. Factual Background

What is an interchange ?*

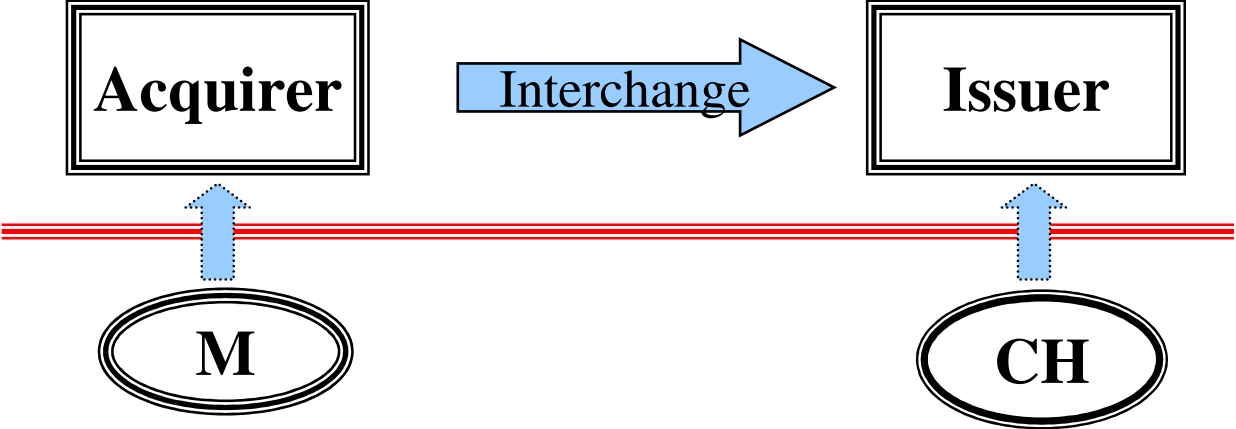
- Cost allocation devise
- Set on objective and verifiable criteria
- Interchange = Interbank agreement
- Commercial freedom at issuer/acquirer level
- As such, commercially neutral

*based on long standing Jurisprudence from the European Commission



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I. Factual Background

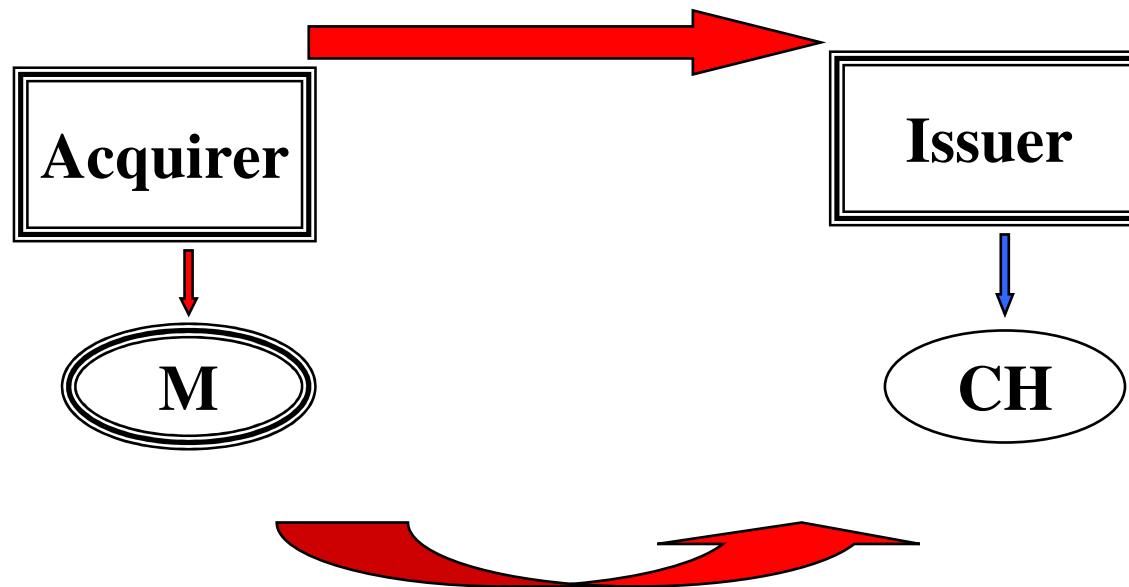


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II. Interchange fees and EC Competition Law

Initial position of the EC (until Sept 2000)



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EC . 2000 - The U Turn

A. EuroCommerce Lobby

Interchange fees = unjustified profit for issuers

- Merchants are financing advantages provided to cardholders (mileage, insurance...)
- No objective justification

→ “Should be forbidden”

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EC . 2000 - The U Turn

A. EuroCommerce Lobby (cont'd)

If Interchange fees are not forbidden,

- should only cover processing costs (not cover the guarantee)
- components must be known and regulated
- guarantee should only be an option,



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EC. 2000

B. Revisited position of the Commission (on the Visa case)

- The clients' captivity allows for abuses without sanctions
- No objective cost justification
- No Interchange = Direct Tarification ◆
- (-) 80% MSC



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2000

B. Revisited position of the Commission

- Multilateral Interchange fees are not necessary (e.g.ec-karte)
- Direct tarification should be preferred
- **Guarantee = joint offer** ◆ **should be optional**

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The 2nd U-Turn - July 2002

On 24th July, the EC changes its mind again:

- Interchange fees restrict competition
- but **can be exempted** if they produce “beneficial efficiencies and economies”

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The 2nd U-Turn - July 2002

- Visa has presented a “package” in which:
- It reduces the level of its interchange
 - 0.7% for deferred and credit cards by 2007
 - 0.28 Euro for debit cards
- Interchanges will be capped to costs based on a cost study.
- Merchants will be told about the level of interchange fees



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The 2nd U-Turn - July 2002

This decision has been criticized because:

- The reduction of rate has intervened before any cost study
- a flat rate is applied to debit cards (quid cost of fraud).



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III. The way forward

- Independent of the Visa move to save its interchange,
- There are other ways to defend interchange fees



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III. The way forward

Introduce a proper methodology

Coherent, objective and defensible (debit/credit)

↓ At cross-border level

↓ In every country

Based on objective cost studies.

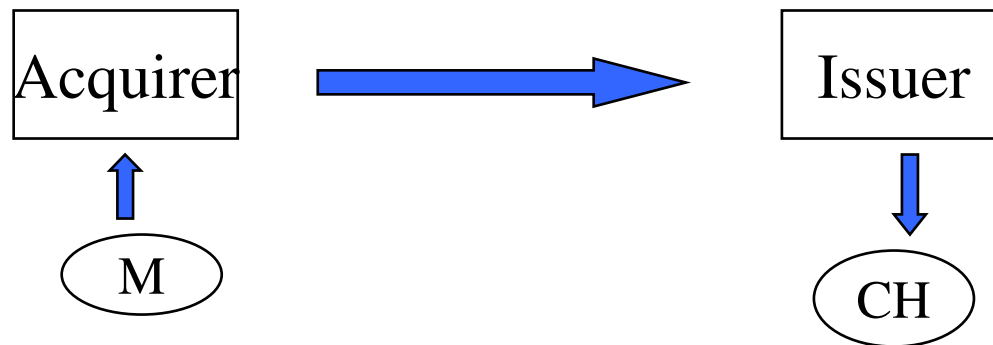
Change programs can be implemented quickly

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III. The way forward

2. End cross-subsidization

Introduce a proper tarification at both ends (CH and M), as a complement to interchange: New tarification patterns to maintain profitability



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Interchange Fees - Conclusion

- ↓ Interchange can be saved, both for credit and debit
- ↓ Introduce the necessary corrections, gradually but quickly
- ↓ To send the right message from within the industry

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Interchange fees, the best way to pave the future

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Interchange fees, the best way to pave the future

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