PAYSYS REPORT

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In this issue:

1. Drastic anti-cash regulation: the future is in cards?
2. Surcharge I: Brexit
3. Surcharge II: PayPal (Flixbus)

Contents

1. Drastic anti-cash regulation: the future is in cards?

In the recent past, both India and Greece have taken drastic steps to reduce the use of cash. India took the two most widely used banknotes out of circulation and replaced them only with a time lag. As a result, card usage soared. But this effect was just a one-off. The current growth rate of card usage is the same as before. Greece restricted access to cash for a certain period and has required merchants to offer card payments. This has been a game changer. The growth rates of card usage figures have jumped up. As a consequence average card usage per person in Greece may soon be higher than in Germany. But the card industry should refrain from demanding "Greek style" measures. In the end, such a policy would lead to even more regulation of the card market.

2. Surcharge I: Brexit

In the UK, Doomsday scenarios for a non-deal Brexit are popular. One issue is the "Brexit tax" for UK cardholders shopping in the reduced EU, charged by merchants with surcharging fees. Brexit could damage some main benefits of the PSD2. Several fake figures are making the rounds in the public debate. In fact, card holders are unlikely to suffer from a Brexit tax. Rather, UK acquirers and continental merchants may have higher costs whenever Brits shop on the continent. The UK Government is preparing for a possible no-deal Brexit through several legislative proposals in order to operate effectively in the payments sector and to mitigate the negative effects for card payments. At the same time, the Commission is dealing with Mastercard and Visa in order to extend the regulation of the interchange fees to incoming cards payments from outside the EEA, which could be relevant for the UK too.

3. Surcharge II: PayPal (Flixbus)

There is a first court ruling on the surcharging ban, which has been in force within the EU for most common payment instruments since 13 January 2018. A court in Munich has forbidden the transport company Flixbus to charge additional fees for a payment via PayPal and Klarna. The court surprisingly regards the e-money system PayPal as a four party payment card scheme. The obviously uninformed judgement leads to considerable confusion.

Drastic anti-cash regulation: the future is in cards?

(mk) In recent times, we have seen some drastic government action against cash. In November 2016 the Indian government embarked on an interesting „payment experiment“. The two most widely used bank notes were declared invalid. They had to be turned in and exchanged against new bank notes. The move was intended to hurt black money and increase the use of cashless means of payment.[1]

In Greece, the amount of cash that could be withdrawn from ATMs was restricted. In parallel, shops were forced to offer non-cash payments. The aim was two-fold, to slow down the flight out of the banking system into cash and to reduce tax avoidance.[2]

Now that the dust has settled it is time to take a look at the effects of these measures on the card business.

Our Comment:

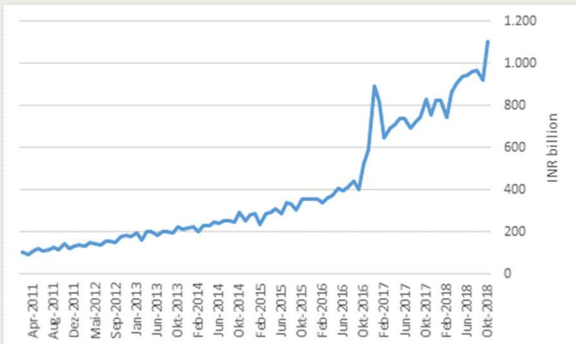
The scale of the Indian experiment can best be inferred from the evolution of ATM cash withdrawals (Figure 1). ATM withdrawals fell from INR 2,551 billion (USD 40 b) in October 2016 to INR 850 billion (USD 13 b) in December. The amount of cash in circulation fell from INR 18 trillion (USD 281 b) in early November to INR 9 trillion (USD 141 b) in early January. However, subsequently, ATM withdrawals and currency in circulation recovered and seem to have returned to their earlier expansion paths.

Figure 1 ATM Cash Withdrawals in India

Source: Reserve Bank of India

Card payments strongly increased from INR 519 billion (USD 8 billion) in October to INR 891 billion (USD 14 billion) in December. After that, they declined to INR 645 billion (USD 10 billion) in February. Subsequently, the value of card payments seems to have returned to the previous growth rate. Thus, there was a „one-off“ pushing card payments up. But as far as currently available data are concerned, growth has not been affected.[3]

Figure 2 Card Payments in India*



*: excluding prepaid instruments:
Source: Reserve Bank of India

As before the experiment, Indian card payments are rising at an impressive rate of about 22% p.a. – albeit from a very low base.[4] A similar observation can be made with respect to card acceptance. The number of POS terminals jumped up after November 2016. But after March 2017, the rate of terminal growth basically fell back to the level experienced in the period 2011 to 2016.

Effects of the bank note replacement experiment have been fairly limited.

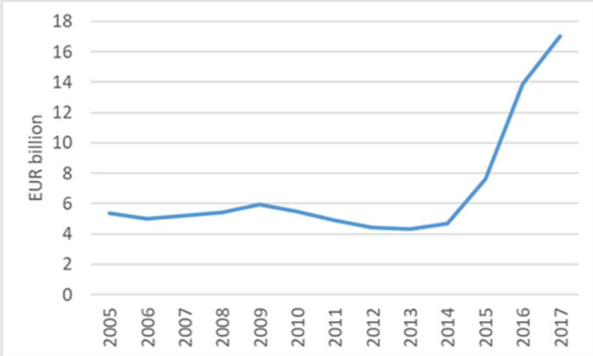
So overall, the effects of the bank note replacement experiment have been fairly limited. Card usage had been low but growth rates were around 20%. This is about the same rate that can currently be observed. Even though the card effect of the 2016 measures looks impressive, looking back in a few years time these changes will be nothing but a small „blip".

The Greek experience differs substantially from the Indian experience. Like India, Greece imposed restrictions on cash. But the form of the restrictions was different. The Greek government imposed maximum amounts for cash withdrawals. A little later it supplemented this measure with the introduction of compulsory card acceptance.

These measures had the desired effect. Card usage at the POS took off (see Figure). Whereas in 2014, the amount of card payment transactions per person was equal to 6, in 2017 it stood at 41. This figure is expected to rise to 60 in 2018. Moreover, 50% of transactions are contactless and 10% are below 10 EUR. This increase has been strongly driven by the expansion of the acceptance base (see Figure).

For the public purse, the results have been equally impressive. VAT income increased substantially.[5] In spite of a declining tax base, VAT revenues rose by 8.5% (Q4-2015), 18% (Q1-2016) and 15.9% (Q2-2016).[6]

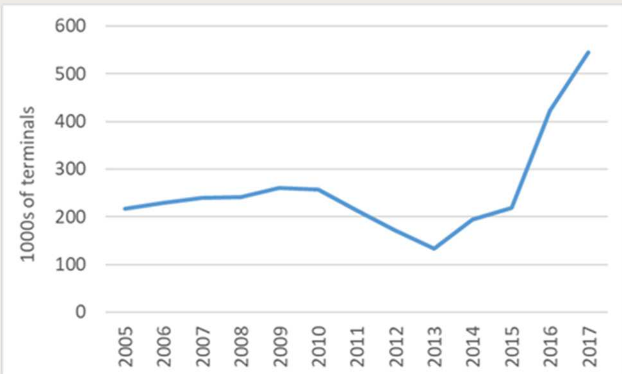
Figure 3 POS Transaction Value in Greece (Greek cards only)



Source: ECB Blue Book data

Regulatory „successes" such as the one in Greece seem to have inspired industry representatives in other countries. In Germany, for instance, Bitkom, the Association for IT, Tele-communications and New Media has published a position paper in which it demands mandatory card acceptance at the point of sale (POS).[7] Bitkom argues that such a measure would provide consumers with „freedom of choice". Nothing is said, though, of potential infringement of merchants' freedom to accept or not accept whatever they choose. The proposal also says nothing about the tricky issue of which brands should be accepted.

Figure 4 EFTPOS Terminals in Greece



Source: ECB Blue Book data

On close reflection, the industry should be careful with such wish-lists. Card payments are already heavily regulated. But don't think that it could not get any worse! In a market with mandatory card acceptance, regulation might get much more onerous. In particular, all PSPs on the acquiring side might become the target of additional rules, including pricing regulations.

Surcharge I: Brexit

(hg) A no-deal Brexit-scenario is still realistic. In order to prepare for this case, the UK government has made a lot of legislative proposals to amend UK law if retained EU law becomes inapplicable after withdrawal of the UK from the EU on March 29, 2019. Especially regarding financial services, the UK Treasury has made several draft "statutory instruments"(SI) to prevent chaos and to ensure a smooth exit, even in case of a non-transitional period. They call it "onshoring" financial services legislation. One SI (published on 16 November 2018)[8] deals with the "onshoring" of the EU Interchange Fee Regulation (IFR 2015). The UK would be beyond the scope of the IFR. The proposal of the HM Treasury mirrors the existing IF caps and most of the rules. However, only domestic transactions within the UK should be subject to the new UK IFR.

As further preparation for a no-deal scenario, the UK government has published since summer 2018 more than 100 "technical notes" with information to citizens and businesses on how to act in case of a no-deal Brexit. In this context the government stated in its "Guidance - Banking, insurance and other financial services if there's no Brexit deal": *"The cost of card payments between the UK and EU will likely increase, and these cross-border payments will no longer be covered by the surcharging ban."*[9] Since the publication of the first batch of these planning papers, accompanied by a speech of the former Brexit secretary Dominic Raab on 24 August 2018, the potential increase of surcharging fees to the extent of 166 m GBP for Britons shopping on the continent is still an integral part of the Doomsday scenario in the British press.

Our Comment:

With the entry into force of PSD2 (Art. 62 Par. 4) on 13 January 2018, the prohibition of surcharging became effective for card payments which are subject to the IF caps according to the IFR (2015/751) as well as for SEPA credit transfers and direct debits. The surcharging ban is relevant for all domestic and cross-border card transactions with capped IF within the EEA. Member States could extend the prohibition optionally to other payment instruments, like PayPal. Up to this date, surcharging by card accepting merchants had been allowed in more or less half of the Member States. However, the size of fees was limited to the merchant´s cost of accepting the payment instrument.

€550 m

From the Commission´s perspective, the prohibition of surcharging for most card payments was one of the most important achievements of the PSD2. It was a central theme of the press release of the Commission of January 12, 2018: *"With PSD2 becoming applicable, we are banning surcharges for consumer debit and credit card payments. This could save more than €550 million per year for EU consumers."* No evidence has been given where this number of €550 m (about 1 € per inhabitant) comes from. In its Impact Assessment analysis of 2013 the Commission says the savings for consumers will be *"part of EUR 731 million annually"*.[10] The amount was probably reduced because in the meantime the IFR (2015) had significantly reduced merchants' costs. Moreover, even after the PSD, surcharging is still allowed for certain card payments (e.g. commercial card payments) and other means of payment (provided that individual Member States have not extended the ban to other means of payment, such as PayPal).

At the same time, the savings for consumers as a consequence of the surcharging ban were intensively discussed in the UK. Here the ban was extended to other consumer payments instruments, such as retail e-money payments via PayPal and the usage of Apple Pay. The Prime Minister Theresa May tweeted on 13

A Genesis of Fake Figures

Survey of ResearchNow (2012)

Merchant questionnaire in 9 MS where surcharging was allowed or (illegally) practiced (France); Results: average surcharge estimate per country and sector and average share of total annual sales per sector subject to surcharging.
Critique:
- no information about size of the sample,
- not including Estonia, Malta, Poland, Slovakia and Slovenia where surcharging was allowed too,
- no independent verification of results.

Study on the impact of PSD2 by London Economics/iff/PaySys (Feb. 2013)
Surcharging in EU: €731 m in 2011
(thereof €451.6 m in UK)

Extrapolation based on the estimates of ResearchNow and sales volume by households per country and sector of Eurostat figures for 2011

Impact Assessment PSD2 and Reg. 924 by the European Commission (July 2013)
Surcharging savings for EU consumers after PSD2: part of €731 m p.a.

The outcome of £166 m is the simple mean value of two estimates. The first estimate is based on the EU impact assessment: 15.97% (UK share of EU nominal GDP) of €731 = £95 m. The other estimation is made by the UK Department for Business, Innovation and Skills (BIS) of £473 m for 2010. This value is reduced by 48% as a result of the IF-caps (12/2015) to £227 m. To the mean value (161 m) a value of 4.5 m is added as estimated surcharging value of other payment means besides cards like PayPal. In its calculation the HM Treasury made several errors:
- it overlooked that the source of the total EU value included a specific share for the UK surcharging of €451.6 (which was not far away from the BIS estimate!),
- it also didn´t reduce the pre-IFR EU figure (€731 m) by 48%,
- the premium for non-card means of payments of 4.5 m is redundant, because these surcharge fees are already included in the EU figure,
- the value is linked to UK payments volumes of 2010/2011 (not 2015!),
- no consideration of card payments, which are not subject to the IF caps (e.g. commercial cards) and can still be surcharged.

Impact Assessment HM Treasury (July 2017)
Surcharging in UK: £166 m (2015)

Press Release European Commission (Jan. 2018)
Effect of PSD2 surcharge ban: „more than €550 m p.a.“

The figure of €550m is not justified by the Commission. Probably a reduction of the 731m due to the IF regulation since 12/2015 and the allowed surcharging of card payments without capped IF (commercial cards, 4-party schemes). However relevant payment volumes increased since 2011.

Public discussion in UK about benefits of PSD2 (Jan. 2018)
Surcharging paid by Britons: £166 m (2015)

Erroneous interpretation by the UK government: £166 m is not „the surcharging cost for Brits in 2015“. It is the estimated surcharging fee volume, charged by UK merchants, which are paid by all consumers (including foreign cardholders). Fees paid by Britons outside the UK are not included!

Public discussion in UK after publication of „technical notes“ by HM Treasury in Aug. 2018
Surcharging fees to be paid by Britons for cross-border card payments in the EU: £166 m after Brexit

Totally wrong interpretation of HM Treasury figure by the English press if stating that the 166m are linked to surcharging fees paid by Britons for XB transactions in the EU after Brexit.

“166” looks like an accurate calculation, but isn´t. The figure is far away of being serious

January 2018: *"From today we're banning hidden charges for paying with your credit or debit card – a move that will help millions of people avoid rip-off fees when spending their hard-earned money."* Their critics replied that this is not an achievement of the UK government, but of the EU. Already at that time, fears were expressed that this advantage for British consumers would be cancelled out by Brexit. This fear is of course unfounded, as the British Government is free to maintain the surcharging ban at home after Brexit. The same applies to the regulation of IF and the retention of IF caps for domestic consumer card payments. Even after Brexit, the same rules will apply in the UK with a “UK IFR” as in EU member states that remain subject to the “EU IFR”. A draft law to this effect was presented by the British government on 16th November in the event of a no-deal withdrawal.

£166 m

The surcharging issue popped up in public again after the speech of Dominic Raab, at that time secretary of state for exiting the EU, on 23 August 2018. The Independent headlined: *“No-deal could force UK credit card users to pay £166 m 'Brexit tax', government admits.”* Even foreign newspapers picked up this rumour of a “Brexit tax”.

The source of the £166m figure as total volume of surcharging fees charged by merchants in the UK is the Impact Assessment analysis of the PSD2 produced by HM Treasury in 2017[11]. “166” looks like an accurate calculation, but isn´t. It is the mathematical exact mean value of two very diverging raw estimates for the UK market. And what's more, one estimate is based on an incorrect interpretation of an EU figure by the Treasury. The figure is far from credible due to several other logical and calculation errors made by the Treasury in its analysis (see chart “A Genesis of Fake Figures”).

Whether correct or not, the figure refers to the estimated volume of surcharging fees charged by UK merchants in 2011/2012. On the other hand, the official statement of the UK Government of a “likely increase” of surcharging fees, is related to cross-border card payments between the EU and the UK (after leaving the EU). The further course of the rumor was predictable. Probably the press agency Reuters[12] first created the fake news by combining both pieces of information in its World News of 23 August 2018, citing the government who should have said that cross-border surcharges cost Britons about 166 million pounds in 2015. This “fact” has been in the world ever since. Unfortunately, once the genie is out of the bottle, you can’t get it back in!

Dear Britons, relax! Yes, only cross-border card payments between the EU and the UK will no longer be subject to regulated IF caps (neither by UK IFR nor by EU IFR) and thus to the PSD2 surcharge ban. No, the surcharging fees for XB transactions paid by Britons were and will definitely not be £166 m annually or even a fraction thereof. Yes, after Brexit, merchants on the other side of the Channel will be allowed to surcharge your payments with cards issued by UK banks. However, it is very unlikely that these merchants will penalize your shopping with a “Brexit tax” as they usually do not discriminate against foreign shoppers coming from outside the EU with surcharging today.

Intraregional transactions become interregional

However, the irrational “Angst” in the UK of surcharging leads us to another, much more relevant consequence of Brexit for merchants on the continental side of the EU. As already stated, the existing EU IFR covers consumer card payments within the EU (domestic and XB). After Brexit only domestic card payments will be subject to the proposed UK IFR. Today intraregional transactions between UK and other Member States will then become interregional transactions, not subject to the IF Regulations (EU and UK) anymore. Non-capped interchange fees, which are set by Mastercard and Visa for interregional transactions will apply, like for US or Japanese tourists shopping in Berlin. According to the Mastercard rules, the UK would probably become a part of the so-called “Western Subregion” with its specific IF regime.

As a consequence, for instance IF for credit card XB transactions between the UK and the reduced EU will be again about 1% (instead of 0.3%). IF for XB debit card transactions will increase too. Regarding these XB transactions, all card issuers (EU and UK) will be the winners, all merchants with "IF++" acquirer contracts and all acquirers with blended fee merchant contracts will be the losers. The additional cost for Britons shopping on the EU continent will hit continental merchants and acquirers.

But it doesn't stop there. In Art. 1 Par. 1 the scope of the EU IFR is defined as follows: "*This Regulation lays down uniform technical and business requirements for card-based payment transactions carried out within the Union, where both the payer's payment service provider and the payee's payment service provider are located therein.*"

Transactions of a German merchant acquired by an UK payment service provider will not be subject to the EU IFR after Brexit.

In the TOP 3 of card acquirers active in the EU two giants are UK companies: Worldpay and Barclays Bank. Worldpay is a particularly important player outside the UK. For instance, the transactions of a German merchant acquired by a UK payment service provider will not be subject to the EU IFR after Brexit, flagged as interregional transactions with a non-capped IF. Only its transactions made by cards issued in the UK could be regarded as domestic transactions, subject to the new UK IFR. Internationally active UK acquirers have to follow other PSPs, which are applying for licenses from competent authorities within continental EU member states to prevent this significant disadvantage for their merchants outside the UK. I guess they are already taking preventive action.

New IF deal for interregional card transactions between EU and Mastercard/Visa

However, another realistic scenario could also mitigate these unpleasant effects of Brexit regarding IF as described above. On 4 December 2018 the Commission announced a planned deal with Mastercard and Visa regarding the capping of IF for incoming interregional transactions of consumer debit and credit cards issued outside the EAA.[13] The details of the "voluntary" offers of both schemes were published in the Official Journal of the European Union (C 438/11 of 5 December 2018). The schemes would align the IF caps for incoming interregional transactions of consumer cards to the existing caps of the EU IFR, however only for card-present payments. For card-not-present ("online") transactions the caps will still be high: 1.15% for debit and 1.5% for consumer credit cards issued outside the EEA.

The Commission says in its Press release, the deal "*would reduce the inter-regional MIFs by at least 40%*". Obviously the proposed caps are relevant for MIFs (Multilateral IF) of the schemes and not for all IFs (including bilateral IF) as being subject to the EU IFR. After a no-deal Brexit the UK will not be part of the EEA. At least the MIFs for incoming interregional card payment transactions (card issuer in the UK or elsewhere outside the EEA) at a merchant outlet in the EAA will fall within the scope of the proposed caps.

The agreement shall enter into force six months following the date on which Visa and Mastercard receive formal notification of the Commission decision and would apply for a period of five years and six months. The Commission has started a consultation period, which will end on 5 January 1919. However, the agreement will thus not be immediately relevant after 29 March 1919 (expected Brexit day).

Surcharge II: PayPal (Flixbus)

(hg) The surcharging ban for several payment instruments has now been legally binding in all Member States for about 12 months since January 13 2018. It is the result of the implementation of the PSD2 (Art. 62 Par. 4):

"In any case, Member States shall ensure that the payee shall not request charges for the use of payment instruments for which interchange fees are regulated under Chapter II of Regulation (EU) 2015/751 and for those payment services to which Regulation (EU) No 260/2012 applies."

Thus since at least this date merchants (and other payees) have not been allowed to surcharge consumers for payments with the most common card products: credit and debit cards of the so called four-party card schemes (Mastercard, Maestro, Visa, V PAY and domestic card schemes) if the card is issued in the EEA and for which the interchange fees are regulated. The relevant payment instruments of Reg. 260/2012 are credit transfers and direct debits in euro (SCT and SDD). Member States have the option to extend the ban to other payment instruments (according Art. 62 Par. 5). We already mentioned in the previous article the extension of the ban to PayPal in the UK.

However, in Germany and in several other Member States, the surcharge is limited to the instruments according to Par. 4. In the legislative process, the extension to PayPal was discussed, but the German parliament agreed not to implement it. Nevertheless, the German "Wettbewerbszentrale"[14], a large self-regulatory institution for enforcing the law against unfair competition, initiated a model lawsuit against the company FlixMobility GmbH, an international provider of bus transport services (Flixbus), and against a Dutch chemist's internet shop for surcharging the use of PayPal. In the proceedings against the provider of Flixbus (in which also the surcharges for the payment service "Sofort" (Klarna) were criticized) a first judgment was announced on 13 December by the court (Landesgericht Munich)[15]. The judge is of the opinion that both PayPal and Sofort fall under the surcharge ban according to Art. 62 Par. 4 of the PSD2 (implemented in German law).

Our Comment:

Why does a court dare to make a judgment when its knowledge obviously relates primarily to Wikipedia knowledge (quoted several times in the judgment)? Should a legal assessment be based on the mere perception of an average consumer or on the legal facts of the respective case? These are the questions one asks oneself when reading this judgment of the Munich court in detail.

Some basics of PayPal

PayPal (PP) is regulated in the EU as an e-money system, subject to the EU Second E-Money Directive (2009/110/EC). The funds in the PP-accounts of the payer and the payee are e-money. E-money is per definition "prepaid". It is issued "on receipt of funds". In the PP scheme, e-money is issued via the exchange of "traditional" money (using a current bank account) or even by other e-money products (e.g. prepaid card). The instrument to transfer traditional money to the PP-account ("funding the account") can be a direct debit, a credit transfer, a debit or a credit card.

The other way to get a credit balance on the account is by receiving e-money from other PP-accounts (e.g. for selling products or as a gift). The only way to use a PP-account is to transfer money to other PP-accounts or to cash it out (re-exchange in traditional money). If the balance is zero or not sufficient to make an e-money-transfer to another PP-account, the payer account must be funded first (e.g. by credit transfer from a bank account to the bank account of PP, which transforms the value into e-money by crediting the PP-account). Negative balances are not allowed (e-money = prepaid). For a user the system is ingenious, but actually quite simple.

Many account holders use the payment service when their account balance is zero. In this case, two transactions are generated one after the other: a funding transaction from the PP account (e.g. by credit card or direct debit) and a subsequent e-money transaction to the PP account of the merchant. For the consumer (including Bavarian judges) it looks like a single credit card or direct debit transaction.

However, this is only a perception that does not correspond to the legal facts. The merchant receives a PP-payment that is subject to the terms and conditions of the PP-system. In this case, he definitely does not accept a payment by credit card or direct debit. He even has no idea how the PP-payment was "funded" by the payer. It is similar to a transfer from one bank account to another. In this case, it is irrelevant to the legal nature of the credit transfer which payment instrument was used initially to transfer the money to the original account (bank transfer, direct debit, cash deposit, cheque, etc.).

The judgment confuses the whole EU Regulation of e-money.

The Court´s perspective

Now the court merges the two transactions into one transaction and applies the legal status of the funding transaction to the PP-transaction (even in case of no initial funding transaction). The judgment refers to the frequency of funding through payment instruments subject to the surcharge prohibition (SCT, SDD and credit card). The Court says that "*as is generally known*" "*a variety of people*" use these instruments. However, there is no publicly available data on how often and with which payment instrument a PP-payment is "funded" in advance of the PP-transaction.

Secondly, the PP-account can also be topped up by cards that are not affected by the caps of the IFR: cards, issued in 3-party schemes, commercial cards or cards issued outside the EAA. Thus, the alleged majority of non-surchargeable payment instruments used for funding determines the legal character of all subsequent e-money transactions, even if the transaction is made from a credit balance. That's serious stuff. It would confuse the whole EU Regulation of e-money.

The court goes even further. Since the IF caps only apply to cards in 4-party schemes, the court simply declares PayPal to be a four party payment card scheme according to the IFR, if a credit card is used for funding.

Remember: What is a four party payment card scheme? Art. 2 Par. 17 of the IFR (2015/751) says:

"'four party payment card scheme' means a payment card scheme in which card-based payment transactions are made from the payment account of a payer to the payment account of a payee through the intermediation of the scheme, an issuer (on the payer's side) and an acquirer (on the payee's side)."

The Court says that, besides the consumer (payer) and the merchant (payee), the third party is the issuer of the credit card used for funding and the fourth party is PayPal as acquirer. PayPal is definitely not the merchant´s acquirer of the card transaction. It is completely irrelevant whether the PP-accepting merchant accepts credit cards or not. PayPal is according to the Court´s decision also the involved payment card scheme. I assume Amex, Mastercard, Visa & Co would not like this legalized friendly takeover of their schemes by PayPal.

What are the realities?

For the initial transaction, for instance a Visa branded card transaction, PayPal is the merchant (not acquirer), the acquirer is probably Worldpay (for PayPal Europe) and Visa is the payment card scheme. For the second transaction, PayPal is issuer, acquirer and scheme owner of the e-money based instrument (three party). Even if the court turns two transactions into one, only the terms and conditions of one scheme can apply to this merged transaction: PayPal or Visa.

The only clean way to prevent surcharging of PayPal transactions is to extend the surcharge ban by law according to Art. 62 Par. 5 PSD2. Furthermore, PayPal has the possibility of prohibiting surcharging of its merchants by contract (which is usually already given). Declaring the e-money scheme PayPal as a four party card scheme according to the IFR misjudges the legal situation and can have unwanted far-reaching consequences for PayPal and other e-money schemes.

The only clean way to prevent surcharging of PayPal transactions is to extend the surcharge ban by law according to Art. 62 Par. 5 PSD2.

Google Pay & PayPal

In October 2018, Google Pay and PayPal announced the possibility of adding PayPal into the mobile wallet of Google Pay. It is part of the PayPal strategy to enter the sector of contactless payments at the physical POS. By choosing PayPal as means of payment in the Google Pay wallet the consumer thinks he's generating a PP-transaction. That is not the case. PayPal issued a virtual debit card (Mastercard) which is linked to the PP-account of the payer. Otherwise, he could only use this wallet application at merchants who accept PayPal at the till (which are very rare). If the PP-account is zero, the PP-account will be funded by a direct debit to the bank account that is linked to the PP-account.

Anywhere where contactless Mastercard payments are accepted, can now be paid in this way. How? On PayPal's[16] website, PayPal is characterized as "*standard source of payment*" for a payment by Google Pay. Elsewhere on the website it says, PayPal is the "*payment method*", which is added to Google Pay. And: "*You pay in the shop with Google Pay.*" Pretty confusing, even for Bavarian judges. It is like Russian dolls.

Which payment instrument is used in this case to make the payment between the customer and the merchant?

a. Google Pay
b. PayPal
c. Mastercard
d. Direct debit

In the consumer´s perception, probably Google Pay and PayPal. The Munich Court would go for direct debit. However, from a legal point of view, the correct answer is c. The transaction is made by a debit card, issued by PayPal, which comes under the rules and regulations of the four party card scheme Mastercard. Don´t worry, the transaction cannot be surcharged by the merchant.

Klarna/Sofort

For the court, a Payment Initiation Service (PIS) via Klarna (Sofort) is basically a SEPA credit transfer and is therefore also subject to the surcharge ban. Klarna is, however, an additional service for which the merchant pays a fee to Klarna. For the payment initiated by Klarna via credit transfer, the merchant pays an additional bank fee if necessary. It is undisputed that the merchant may not charge these bank fees via surcharging to its payer.

The overlay services, Payment Initiation Services (PIS) and Account Information Services (AIS) came under the scope of the regulation with the new PSD2. However, the PSD2 clearly differentiates between the execution of a credit transfer and the provision of a PIS. Usually the service is offered to the merchant by two different PSPs. In addition, a PIS (or AIS) is not a payment service to which Regulation 260/2012 applies.[17]

The argument of the court is based on the non-existent contractual relationship between Klarna and the payer. It concludes that Klarna only provides an additional service to the merchant (credit check and direct information that the transfer has been made).

However, the charging of a fee only on the merchant's side is based on Klarna's business model. A fee could also be charged to the payer, who also has the advantage of an additional service. If the payer initiated a plain credit transfer without Klarna, he would have to start a separate online banking session. In addition, he must enter the purchase data (e.g. invoice number) as a reference and wait until the merchant notices the credit at its merchant account at some point.

This would slow down ecommerce shopping considerably. There is therefore no reason why the merchant (who bears all the costs) cannot pass on this customer advantage through surcharging. The simplest way to avoid a legal dispute would be to add a plain credit transfer to the payment methods offered by the merchant in addition to the diluted credit transfer via a PIS. In this case, the customer can switch to a widespread payment instrument “credit transfer” that the merchant may not surcharge.

In our opinion, the judgment of the Munich court is a little too disruptive. It is to be hoped for the whole payment industry and its regulators that the operator of Flixbus will appeal. This legal confusion cannot be allowed to establish itself without contradiction.

Notes

1 See: „India: De-Monetisation or Demon-Etisation?“ in the 8/9-2016 edition of this newsletter.
2 See: „The Interchange Fee Regulation and the Greek way to trigger a less-cash society“ in the 3/4-2017 edition of this newsletter.
3 Note that the strong increase in October 2018 is mainly due to seasonal effects.
4 Prepaid instruments (mostly mobile wallets) also received a push. In December 2016, the value of payments with these instruments almost doubled. But after that the volume of payments stagnated before returning to high growth in the summer of 2017. In October 2018, the value of payments with prepaid instruments reached INR 220 billion (about 20% of the value of card payments).
5 See Volker Schloenvoigt: Interview With George Drimiotis, CEO of Cardlink, November 30th, 2018. (https://edgardunn.com/2018/11/interview-with-george-drimiotis-ceo-of-cardlink/)
6 Year-on-year figures. See George Hondroyiannis, Dimitrios Papaoikonomou: The effect and of card payments on VAT revenue in Greece, Bank of Greece Working Paper 225, May 2017.
7 Bitkom-Thesen zur Wahlfreiheit beim Bezahlen, 16. November 2018. (https://digitalwahl.de/sites/digitalwahl/files/2018-11/181116_Bitkom-Thesen%20zur%20Wahlfreiheit%20beim%20Bezahlen.pdf)
8 https://www.gov.uk/government/publications/draft-interchange-fee-amendment-eu-exit-regulations-2018
9 https://www.gov.uk/government/publications/banking-insurance-and-other-financial-services-if-theres-no-brexit-deal/banking-insurance-and-other-financial-services-if-theres-no-brexit-deal (updated 19 December 2018)
10 https://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX:52013SC0288 (p. 77)
11 https://www.gov.uk/government/consultations/implementation-of-the-revised-eu-payment-services-directive-psdii, p. 35-40
12 https://www.reuters.com/article/us-britain-eu-notices-finance/britons-living-in-eu-could-lose-access-to-uk-bank-services-in-no-deal-brexit-idUSKCN1L8181
13 http://europa.eu/rapid/press-release_IP-18-6655_en.htm
14 Zentrale zur Bekämpfung unlauteren Wettbewerbs Frankfurt am Main e. V. (www.wettbewerbszentrale.de)
15 File reference: 17 HK O 7439/18 (not online available)
16 https://www.paypal.com/de/webapps/mpp/google-pay#
17 See also Art. 1 Par. 3 of this Regulation: 3. “*Where payment schemes are based on payment transactions by credit transfers or direct debits but have additional optional features or services, this Regulation applies only to the underlying credit transfers or direct debits.*”

We wish all our readers a Happy New Year!

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