

Topics of this issue:

- 1. End of no-surcharge rules?**
- 2. Visa Europe is pushing cash-back**
- 3. German conflict over direct debit**

1. End of no-surcharge rules?

Article 52(3) of the PSD rules that surcharging should not be prevented by payment systems rules. However, it gives member states the option to allow no surcharge rules:

“The payment service provider shall not prevent the payee from requesting from the payer a charge or from offering him a reduction for the use of a given payment instrument. However, Member States may forbid or limit the right to request charges taking into account the need to encourage competition and promote the use of efficient payment instruments.”

The German government does not seem to wish to use this option and is likely to implement the prohibition of no-surcharge rules. Accordingly, German banks are already under way to change the rules of the German debit scheme which so far have included a no-surcharge-rule. In the future, merchants will be allowed to offer discounts for cash payments.

Our comment:

For the moment, we do not know how the issue of no-surcharge rules will be dealt with in the other EU countries. However, abolishing no-surcharge rules may well become common practise. MasterCard made its mark in 2006 when it decided to abolish the no-surcharge rule within its scheme. The question is, however, what will be the implication of permitting surcharging. There is a wide believe that surcharging is costly and that it is not widely used – even if permitted. Two reports commissioned by the EU Commission seemed to support this view. In two countries in which surcharging was allowed by law, Sweden and the Netherlands, surcharging was not widely used. Recent evidence from Australia suggests, however, that abolishing the no-surcharge-rule may make a difference. After the Reserve Bank of Australia permitted surcharging in 2003, it has been rising significantly – although merchant rates were falling from about 1.45% in 2003 to about 0.8% in 2007.

Merchants Surcharging Credit Cards in Australia

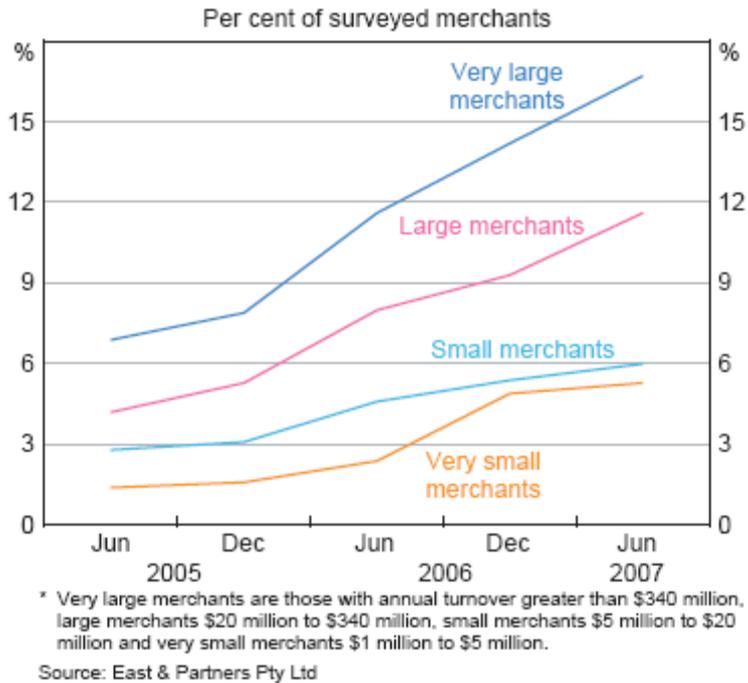


Chart copied from Payment System Board: Annual Report” 2007, p. 25.¹

The chart also shows that surcharging merchants remain a minority. Still, if surcharging is allowed in Europe, one should expect to see more surcharging in Europe – unless, of course, merchant charges will dramatically fall due to the interchange decision of the European Commission. In this case, it will be interesting to see whether merchants will introduce surcharges on cash payments. After all, if the research results of the cards’ associations are to be believed, cash is hugely expensive for merchants.

2. Visa Europe is pushing cash-back

Visa Europe promotes cash-back at the point of sale. “Cash-back” is defined as a pay-out of cash together with a purchase transaction. Basically, a card holder “buys” goods and cash and pays by card. Cash-back is used already in many countries such as Norway, the Netherlands, the UK or the US. In spite of SEPA, the idea is to implement cash-back as a national service. Currently, German banks are discussing whether to implement cash-back as a Visa service. Moreover, the technical specs of the German debit scheme already include cash-back. Thus, in the future, cash-back may also be offered as an ec cash/Girocard service.

¹ See http://203.34.60.68/PublicationsAndResearch/PSBAnnualReports/2007/Pdf/2007_psb_annual_report.pdf

Our comment:

Cash-back may be a coming theme in the EU. In some countries it is used intensively, already. For merchants it is a convenient tool to offer customers an extra service and, possibly, lower cash costs. The future uptake will depend on three factors, however. First, pricing is an issue. In Europe, cash-back flourishes where systems are employed with a per transaction fee. With such pricing, cash-back does not involve an extra fee for merchants. If there is an ad valorem fee and if this fee is also applied to cash-back, this can be a show stopper.

Second, regulation may be an issue. In spite of all the SEPA activity, there are persistent differences in the regulation of payments within the EU. In some countries, cash-back does not require any additional regulatory approval. In others, there are relatively high hurdles. Thus, in Germany cash-back is interpreted as a credit of the merchant to the card holder. Therefore, a merchant needs an exemption from the requirements of the German banking law. In the past, such an exemption has been given, however, only with constraints attached that make cash-back less useful (minimum purchase amount of 20€ and maximum cash amount of 100€). Moreover, the exemption applied to cash-back based on ec cash – a system with PIN authorisation and virtually no risk for merchants.

Finally, on the issuing side, there may be conflicting interests. On the one hand there are banks with few or no ATMs and branches. These banks have a big interest in cash-back because it makes them less dependent on their competitors' ATMs. On the other hand, there are those banks with large networks that do not want to help their competitors. This conflict of interests may well slow implementation of cash-back in some countries.

3. German conflict over direct debit

On May, 8th 2008 the German ministry of finance put a note on its website with the headline: "In the future, the German direct debit will remain a viable payment option" (Deutsches Lastschriftverfahren bleibt auch in Zukunft Zahlungsmittel).² It stresses that many consumer, trade and industry associations are opposed to using SEPA Direct Debit. The note concludes that both types of debit (German and SDD) will be likely to co-exist for the foreseeable future. In talks with the press, representatives of the ministry of finance added that it was never the

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http://www.bundesfinanzministerium.de/nn_54004/DE/Buergerinnen__und__Buerger/Alltag__und__Ehrenamt/002__lastschriftverfahren.html

government's intention to impose a legal deadline for the migration to SDD. This process should be left to the market.³

In response to the government statement, the Bundesbank and the ECB restated the necessity to set a compulsory end date for national payment schemes. Hans Georg Fabritius, member of the executive board of the Bundesbank, stated in an interview that from the point of view of the Bundesbank and the Eurosystem a compulsory deadline was indispensable. Such a deadline could be set by the banks themselves or via public regulation.⁴

The German Retailing Association (HDE) immediately took issue with the position of the Bundesbank. Once more, German retailers stressed the importance of a debit schemes that can be used at the POS. Without such a possibility, there would be less competition and retailers would be entirely dependent on banks' debit card or credit card systems.⁵

Our comment:

From the start, it was obvious that it would not be easy to find a solution for a European direct debit product that would suit all interested parties. Too big are the differences between the national products. Moreover, in some countries direct debits are used for clearing of debit card payments in others they are not. SEPA Direct Debit was a compromise. However, on the side of customers, there seems little enthusiasm to implement the new product. This is particularly true for Germany, one of the heaviest users of direct debits. In December 2007 German corporates wrote a letter to the EPC, complaining, inter alia, about the high costs of mandate conversions. Retailers repeatedly complained that the use of card-initiated direct debit at the POS (ELV) would no longer be usable with SDD. Now, these voices received the backing of a political heavy weight: the German ministry of finance. This is very important because SEPA is, in the end, a politically driven process. The intervention of the ministry makes it much more likely that there will be a co-existence of national and SEPA products beyond 2010.

So, what are the possible solutions to safeguard the initial idea of SEPA? Hans Georg Fabritius pointed out to current initiatives that would make it easier (and cheaper) to convert direct debit mandates. If implemented, such a move would reduce the opposition of large corporates. Retailers' fears could be reduced by introducing a SEPA direct debit for cards.

³ See Marietta Kurm-Engels: Streit über Lastschriften, Handelsblatt, 19.5.2008.

⁴ Im Gespräch: Hans Georg Fabritius, Mitglied im Vorstand der Deutschen Bundesbank „Das deutsche Lastschriftverfahren kann nicht bleiben“, Frankfurter Allgemeine Zeitung, 26.5.2008.

⁵ <http://www.einzelhandel.de/servlet/PB/-s/fkfuvb11y9ahldh932ozf5c2m16zc2ur/menu/1084905/index.html>

Such a direct debit would empower retailers to develop their own schemes without much bank involvement. That is why retailers generally like the idea and banks mostly were against it. However, German banks have changed their mind because they have witnessed that the possibility of retailers to use simple direct debit at the POS (competing with the banks' card scheme) does reduce the pressure from anti-trust authorities. Of course, the topic would be more favourable from the point of view of banks if a general interchange for direct debits would be approved by the European Commission.

The issue of a direct debit for cards is also important for bank-owned card payment systems. At the moment, some national schemes simply use the national direct debit schemes for clearing and settlement. If SEPA does not provide direct debit solution capable to clear card transactions, then banks have to use something else. Either a dedicated system for settling card transactions or they have to use credit transfers. Of course, Visa and MasterCard have their own dedicated clearing and settlement systems. But any new contender, be it EAPS, Monnet or Payfair, would have to come up with something.

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