

2 September 2024

Commerce Commission
PO Box 2351
Wellington 6140
New Zealand

Email: RetailPaymentSystem@comcom.govt.nz

Dear Sir/Madam

Re: Retail Payment System – Costs to Businesses and Consumers of Card Payments in New Zealand

Background

I am writing to you regarding the Commerce Commission's (ComCom) Consultation Paper entitled '*Retail Payment System – costs to Businesses and Consumers of Card Payments in New Zealand*' (referred to as "the Consultation Paper").

The Consultation Paper focuses on the fees paid by New Zealand businesses to accept card payments and the flow-through to surcharges paid by consumers. While the ComCom has outlined a number of pathways forward, BusinessNZ wishes to focus on a few key elements to ensure the ComCom is taking into account all possible solutions.

Cost of Card Payments in New Zealand

Figure 2.2 of the Consultation Paper outlines the main components that make up the merchant service fee charged to receive Mastercard and Visa card payments. Proportionately, the interchange fee (fees paid by the merchants' acquirer to the customer's card issuer for each transaction on the Mastercard and Visa networks) and scheme fee (paid by the acquirer to the relevant scheme network (Mastercard or Visa)) are clearly the two key components. With the former making up 59% of total merchant service fees paid per annum for Mastercard and Visa card payments, this represents a significant proportion of the merchant service fee and justifies a proper examination of its effects on customers, businesses and card providers.

Open Banking

We note that page 15 of the Consultation Paper mentions open banking providing an innovative alternative to Mastercard and Visa. However, this is viewed "*as a medium to long-term solution to greater efficiency within the retail payment system.*"

BusinessNZ examined open banking in 2021 in response to MBIE's Issues Paper that looked at regulatory options for reducing merchant service fees. We have long held the view that there is a rapidly-growing opportunity for the private sector to harness new digital frameworks to improve business-to-business and business-to-consumer transactions and information sharing. Back then, we urged caution in not jumping the gun when considering heavy-handed regulation, since technological advances can rapidly make such approaches obsolete. In some cases, regulatory intervention can delay the speed of innovation uptake, while in others, it can even block technological innovation altogether.

We still take the view that open banking has more potential to provide competitive discipline on fees over the long term than a regulatory clampdown on existing mechanisms. It should be noted that we are now three years on from the MBIE Issues Paper, and it may be the case that once the full consultation period for the Retail Payment System is over, the decisions and intervention logic arrived at may not necessarily represent the best course of action, given other projects at play. Page 16 of the Consultation Paper mentions recent work on the designation of the interbank payment network, which seeks to confront barriers to new payment options that are likely to be more secure, convenient and reduce costs for businesses and consumers.

BusinessNZ recognises that in many areas where new technological options are being considered, not all options will get close to providing a solution. In fact, many will fail, disappointing those hoping for a long-term and sustainable result. However, eventually, one or more alternative solutions will provide an optimal way forward. At the very least, we would want the ComCom to be conscious of alternative technological solutions if the policy process for retail payment system regulation is explored further.

Recommendation: If the policy process for retail payment system regulation is explored further, the Commerce Commission is cognisant of related digital developments that may supersede the need for more heavy regulatory options.

Small Business Merchants

BusinessNZ agrees that small business merchants are more likely to bear higher interchange fees than larger businesses due to a lack of bargaining power with their acquirers, given the small volumes and values of their transactions. However, asymmetry of knowledge and information is nothing new when comparing the size of businesses. Smaller sized businesses are not, and never will be, on a level playing field with larger businesses, mainly due to the additional resources of capital and labour the latter possess. However, if we look further afield, it can be argued that

large New Zealand businesses face the same kind of issues when competing with much larger offshore enterprises.

BusinessNZ's membership is very broad, from micro-sized SME enterprises through to large corporates. Balancing the needs and issues of the entire business community can be complex, especially given the general cut and thrust of business competition. BusinessNZ seeks to enable the best outcomes for the business community and the New Zealand economy overall, and this often entails examining issues broadly in pursuit of a regulatory environment to best foster economic growth.

Wide Range of Interchange Fees

As paragraph 3.4 of the Consultation Paper points out, while interchange fees are a significant cost component of the merchant service fee, there are also hundreds of interchange fee categories across Mastercard and Visa. As the Paper states, *"this impacts the cost and transparency of the merchant service fee paid, merchant service fee pricing and the accuracy of merchant surcharging."*

However, as paragraph 2.11 of the Consultation points out, the revenue from interchange fees also provides benefits to merchants and consumers, by way of card issuers paying rewards, covering fraud losses, assisting in anti-fraud investments and paying other fees. Given the outcome of fraud can have significant financial consequences on those affected, it is important to recognise that elements of the interchange fee can provide a certain degree of security and safety for merchants and consumers. In addition, reducing complexity of the retail payment system also means providing retailers with certainty around when changes to surcharge rates would be expected and avoiding making changes too frequently.

Yet, as paragraphs 3.5-3.13 of the Consultation Paper outline, the inherent complexity and distortive outcome of interchange fees has led to distortions. These include inconsistency in surcharging practices, cross-subsidisation across card types, difficulty in understanding the full implications of accepting different forms of payments, and not all terminal providers providing merchants with the ability to have multiple surcharge rates. Therefore, from BusinessNZ's perspective it is not surprising that this lack of clarity and consistency has led to an average surcharge imposed by merchants being greatly in excess of what they are actually being charged, thereby creating further inefficiencies. This means the task of addressing interchange fees requires examination of a broad range of potential solutions rather than a simple focus on one option.

Options to Address the Issues

When BusinessNZ submitted on regulation aimed at reducing merchant services fees in 2021, the associated issues paper that MBIE produced examined potential options to address the issues through two main avenues. First, specific approaches that would see a change to the fees themselves, and second, a range of supplementary options including taking a 'systems' approach to retail payments regulation. However, this

broader 'systems' consideration seems to be missing from the current Consultation Paper.

We note that the Consultation Paper "*outlines the various methodologies used for determining appropriate levels of interchange fees and considers the rationale for variability across current interchange fee caps.*" BusinessNZ is not in a position to provide expert feedback on the various methodologies outlined in the Consultation Paper, including fee caps. However, we do want to provide further thoughts on supplementary options that we believe would provide greater clarity in an area that is very complex for many businesses.

To that end, we note that one of our Industry Association members, Retail NZ, has previously produced a Retail Payments Position Statement that outlines what they see as the main problems with the Retail System, as well as some potential answers for Retail NZ, Retailers, the Government, and Banks/Terminal Providers.

Overall, their Statement provides a broad number of potential solutions including those focused on improved education and transparency, including:

- *Educate retailers and the public about surcharging and the cost of payments, including cash.*
- *Help retailers to understand the interchange and merchant service fees shown on their bank statements.*
- *Advocate for banks to make it easier for retailers to understand the fees they pay so they can easily evaluate whether or not they should recoup costs via surcharging.*
- *Direct all banks to provide statements that outline the retailer's total average fee (both as a percentage and actual dollar cost) across all payment types.*
- *Provide guidance material to promote appropriate surcharging practices and a standardised way for retailers to disclose surcharging to customers.*
- *Ensure anti-money laundering legislation does not hinder progress on achieving a more efficient and transparent retail payments system.*
- *Establish a national programme to educate consumers about merchant service fees.*

From BusinessNZ's perspective, providing options for better information and transparency would be a good place to start, being an approach that falls at the lower end of regulatory imposition. While we consider there may be scope for movement in interchange fees, we consider the examination of a broader range of measures unconnected to the actual level of the fee itself to be equally important.

BusinessNZ expects other submitters to highlight a range of potential solutions as the first part of the review. We believe the range of supplementary measures likely to be outlined by other submitters could provide a basis for future regulatory change to interchange fees. In terms of taking a deep and considered perspective to address relevant policy concerns, BusinessNZ believes these should be considered alongside, rather than separately from, interchange fee change. This would provide an

opportunity for the industry players affected to explain the changes they could make to balance the need for lower fees without a propensity for regulatory overreach.

Recommendation: That ComCom considers a range of supplementary options equally alongside direct interchange fee regulation.

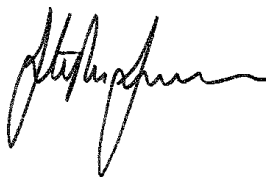
Next Steps

The Consultation Paper outlines possible next steps for this issue after the current review, which includes a draft decision, consultation on the draft decision and a final decision. Depending on the final decision made, those could lead to implementation and new interchange fee levels.

Overall, we are pleased to see the ComCom providing an outline of what processes are to be expected if they decide to move forward with the review, especially since this involves a complicated issue where deep consultation and testing of ideas with those affected in the private sector is required.

Recommendation: That ComCom look to engage with affected parties throughout the consultation period, including testing a broad range of options.

Kind regards,



Steve Summers
Economist
BusinessNZ