

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

ROUNDTABLE ON COMPETITION AND PAYMENT SYSTEMS

-- Note by the Delegation of Norway --

This note is submitted by the delegation of Norway to the Competition Committee FOR DISCUSSION under Item VI at its forthcoming meeting to be held on 24-25 October 2012.

JT03327655

Complete document available on OLIS in its original format

This document and any map included herein are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries and to the name of any territory, city or area.

ROUNDTABLE ON COMPETITION AND PAYMENT SYSTEMS

-- Note by Norway --

1. Structural condition

1.1 *Social costs and benefits of different payment systems*

1. In 2009 the Norwegian Central Bank (Norges Bank) conducted a costs study in the Norwegian payment system.¹ The analysis covered social costs associated with payment cards, giro and cash. The social costs for using and producing these payment services were estimated to NOK 11.16 billion in 2007, equivalent to 0.49 % of GDP.

2. Card payments accounts for about half the social costs, when distributing social cost on cash, cards and giro. The household survey indicated that cash payments accounted for 14 % of the value of payments and 24 % of the number of transactions at point of sale in Norway. Compared to other countries this is relative low figures. In spite of this, cash represented 31 % of social costs. Cards represented 48 % and giros 21 %.

3. The private cost for payments services produced by banks was NOK 7.1 billion in 2007. The corresponding income was NOK 5.2 billion, a cost recovery of 71 %. Income is based on prices per payment transaction and fixed, periodical fees from payers and payees. Cost recovery increased to 87 % when cash services were excluded from the calculation.

4. Calculation of social costs per instrument showed a relatively low per transaction cost of cash payments compared to costs of card payments, NOK 1.80 and NOK 5.93. However, when costs for withdrawals/deposits were included, cash was more expensive per transaction, at NOK 7.06.

2. The Norwegian payment card system

2.1 *BankAxept – the national debit card scheme*

5. The Norwegian payment card system is heavily influenced by the national debit card system BankAxept. BankAxept, owned by banks operating in Norway through the banking association FNO, functions without an interchange fee. Banks operating in Norway (holding a banking licence is a requirement) can join the BankAxept scheme by paying an access fee.

6. Fees in the BankAxept scheme are very low for both merchants and cardholders. Merchants typically pay a per transaction fee between NOK 0.0 – 0.30 and a monthly merchant fee of about NOK 125. Fees for cardholders differ for customers in and outside banks' customer loyalty schemes. In loyalty schemes, customers are given discounts against payment of a fixed annual fee or related to particular accounts or services. At the beginning of 2012, the average annual fee in Norway for BankAxept cards combined with the international card VISA was approximately NOK 208 for loyalty scheme customers and

¹ Norges Bank (2009), "Costs in the Norwegian payment system", Staff Memo nr. 4/2009

NOK 260 for non-loyalty scheme customers. This is an increase of 6% and 9%, respectively, on the previous year. The average fee for goods purchases using BankAxept also rose in 2011 and at the beginning of 2012 was NOK 0.10 for loyalty scheme customers and approximately NOK 1.80 for non-loyalty scheme customers.²

7. The market shares of BankAxept in 2011 were 82 % in number of transactions and 75 % in value. The international schemes corresponding market shares were 17 % and 24 %. At EFTPOS terminals the market share of BankAxept was even higher, constituting 87 % of the number of transactions compared to 11 % of transactions by international cards.³

8. In addition to the low fees, the so-called "preference rule" in the by-laws of the BankAxept scheme is a likely explanatory element of the high number of BankAxept transactions in EFTPOS terminals. The "preference rule" in the by-laws of the BankAxept scheme states that EFTPOS terminals which accept BankAxept card shall give preference to the BankAxept scheme when cards presented at the EFTPOS terminal are cobranded with other payment schemes e.g. Visa or MasterCard.

2.2 *International schemes*

9. The Finance Ministry instructed the Financial Supervisory Authority of Norway (FSA) in 2004, 2007 and in 2011 to conduct a survey of the market for international card schemes and especially to examine the forming and development of the fees, both the interchange fee and the merchant service charge. On all three occasions the FSA was asked to constitute a working group consisting of members from the FSA, the Central Bank of Norway (Norges Bank) and the Competition Authority (Konkurransetilsynet). The following is based on findings in the recent report (the report) published in January 2012.⁴

10. The international schemes operating in Norway are Visa, MasterCard, American Express, Diners Club, JCB and UnionPay. Visa is issued by the bulk of banks operating in Norway (136 issuing banks in 2010), and often cobranded with BankAxept. MasterCard is issued by about 20 banks and finance institutions. American Express is issued by DNB, the by far largest Norwegian bank, and Diners Club is issued by Diners Club Norge. JCB and UnionPay are not issued in Norway.

11. Among the international card schemes the aggregate market shares of the two major card schemes has been stable around 90 % the past decade.

12. There are six acquirers of international card schemes in operating in Norway (2011). The two largest operators Teller and Elavon, who are pure acquirers, acquire Visa, MasterCard and JCB. Teller is the sole acquirer of American Express and UnionPay, as Diners Club Norge is the proprietor acquirer of Diners Club transactions in Norway. The three banks Nordea, Handelsbanken and Swedbank also acquire Visa and MasterCard transactions in the Norwegian market. Teller and Elavon have a combined market share above [50-80 %] (2011).

13. The international card schemes annual growth in volume is double that of BankAxept. In terms of number of transaction the growth of the international card schemes is 60 % higher than the corresponding growth of BankAxept. The difference in actual and potential income from fees in the BankAxept scheme

² Norges Bank (2012), "Annual Report on Payment Systems 2011"

³ Ibid.

⁴ Report to The Finance Ministry by Finanstilsynet, Norges Bank og Konkurransetilsynet (2012), "Vurdering av tiltak i markedet for internasjonale betalingskort i Norge" (Published in Norwegian only).

compared to the international card schemes may induce the banks to prefer the latter and may also hamper innovation and promotion of the BankAxept scheme.⁵

2.3 Policy of fees

14. At present neither the interchange fees nor the merchant service charge of the international card schemes are subject to any direct regulatory measures by Norwegian authorities.

15. The Norwegian Competition Act article 10 is harmonized with TFEU article 101 and EEA article 53. In response to the MasterCard decision by the Commission in 2007 the Norwegian Competition Authority (NCA) opened cases against both Visa and MasterCard in 2008. The cases are still pending. However, the competition rules and the mere possibility that the NCA at any time may enforce them is in itself a passive regulation. The owners of the international card schemes are at any time obliged to comply with the prevailing competition rules.

16. The legal uncertainty regarding the application of competition rules on the determination and fixing of interchange fees has been somewhat amended by the May 2012 General Court ruling in the MasterCard case but will not be clarified until MasterCard's appeal is tried by the courts. Also, economic theory and the discussions regarding the relevant method used to fixing the interchange fee are still in progress. The legal uncertainty and the ongoing evolution of economic theory and method may to a certain degree affect the effectiveness of the enforcement of competition rules.

17. Pending clarity the Norwegian Competition Authority (NCA) choose advocacy towards the Visa and MasterCard card schemes. In addition to monitor the development of the fees in Norway the main focus for the NCA has been to ensure that Visa and MasterCard comply with the conditions agreed upon in their settlements with the Commission and the Payments Directive, i.e. usage of the Merchant Indifference Test methodology, abolishment of no-surcharge rules and the unbundling of merchant service fees.

18. The uncertainty towards legal clarity may induce a need for direct regulatory measures towards the setting of interchange fees in international card schemes. However, the uncertainty of economic theory and method as foundation for a direct regulation will meet challenges equivalent to those present when applying competition rules.

19. Direct regulatory measures will itself lead to a higher level of legal clarity. However, there is a risk of erroneous regulation. Economic theory indicate that there are no guarantees that direct regulation will lead to levels of the interchange fees that are more welfare enhancing than the private setting of interchange fee levels.

20. The Norwegian Ministry of Finance pays close attention to the development of the different fees and executes investigations into questions regarding regulation of the international card schemes at regular intervals, as mentioned above.

2.4 Surcharge

21. After implementation of the Payments Service Directive into Norwegian Law⁶ card schemes operating in Norway is prohibited from denying merchants the possibility of surcharging use of payment cards. However, in the report (2012) the response from the issuers showed that surcharge was used by "none, to a few" merchants, and mostly over the Internet.

⁵ Norges Bank (2012), "Annual Report on Payment Systems 2011", page 8-9.

⁶ The Norwegian Finance Agreement Act, article 39b, first section.

22. The working group behind the report (2012) pointed to the fact that both acquirers and suppliers of EFTPOS-terminals have done little to arrange for the possibility of surcharging. In the follow-up of the report, NETS Norway, the largest supplier of EFTPOS-terminals in Norway, informed the NCA that their Nordic payment solution (Nets Merchant Solutions) support surcharging. However, a specific configuration of the software at each merchant is required for the solution to function.

23. In addition there are other conditions which may impede merchants from surcharging use of payment cards. First, a well arranged and efficient pricing system is costly for merchants requiring additional costs and adjustments to the payments infrastructure, i.e. EFTPOS-terminals. Second, merchants who face competition may have good reasons to assume that price differentiation will deter demand from cardholders and consumers in general. Consumers who experience that price differentiation are troublesome and complicated to relate to will seek to avoid merchants who carry out this practice if there are alternatives, hence leading to loss in sales and revenue.

24. A widespread use of surcharging may require some sort of coordination either by the merchants association or by the large market players. Competition rules that prohibit coordinated agreements that restrict competition may be a hindrance of such an undertaking.

3. Interchange fees

3.1 Structure, level and development

25. Visa and MasterCard use the "issuer-cost" method based on cost studies when setting the interchange fees in Norway. Application of the "merchant indifference test" method on the interchange fees would lead to much higher levels of the fees they argue. The high level of wages and excessive costs of processing in Norway is the main explanatory factors.

26. Results from the report (2012) show that the levels of interchange fees in both Visa and MasterCard have decreased steadily the past decade.

27. For Visa debit cards the average interchange fee has decreased by 8.6 % from 2008 to in 2011. The equivalent interchange fee on credit transactions has decreased by 30 % over the same period. The weighted average of the interchange fee of all Visa transactions have decreased by 15.9 % from 2004 to 2011.

28. The interchange fee as a weighted average for MasterCard consumer cards has decreased by 27.6 % from 2005 to 2011. However, for corporate cards the trend is the opposite with the weighted average of the interchange fee increased by 5.6 % from 2005 to 2011. The interchange fee as a weighted average for all MasterCard transactions has decreased by 19.7 % over the same period.

29. In Norway there is a large distinction between the interchange fees for certain business sectors. The grocery stores typically have a lower interchange fee than other sectors. These differences is likely motivated by some business sectors prolonged reluctance against the international card schemes compared to the BankAxept scheme, with its low fees and widespread use.

30. The major international card schemes have changed the structure of the interchange fees for debit transactions from a pure *ad valorem* pricing to a structure with a *fixed* price plus a lower *ad valorem* element. Based on the prevailing methods for cost calculations of the interchange fees this is not surprising. Debit transactions have a large proportion of fixed costs related to infrastructure. With a high volume the marginal cost of a transaction will approach the average fixed unit cost. In relation to the increasing use of transactions with low amounts a fixed price element may contribute to a more efficient

price structure in the scheme. Transactions with credit cards bring about other cost elements and a price structure with a *fixed* price plus an *ad valorem* element may be more efficient.

4. Merchant fees

4.1 Level and development

31. Findings in the report (2012) show a steady decrease in the merchant service charges (MSC) for Visa and MasterCard in Norway since 2002. With both schemes priced at [2.15-1.85 %] as a weighted average in 2002, the MSC for one scheme has decreased by 35.3 % (2011) while the MSC for another scheme has decreased by 24.9 % (2011).

32. American Express operates with a substantially higher MSC than the other three party and four party schemes in Norway. However, it has had a downward trend decreasing with 12.7 % from 2002 to 2011. For Diners Club the decrease has been more modest with 4.2 % over the same period. JCB however, has increased their MSC by 2.3 % from 2005 to 2011.

33. In the case of the three party schemes the data suggests that the levels of fees have a proportionate development, the MSC decrease when the "issuer rate" decreases, and vice versa. Despite of the lack of intra-system competition the data imply that the MSC's in the three party schemes seems to be influenced by the development in the corresponding MSC's of the four party schemes.

34. Results from the report (2012) indicate that the acquirer's margins have declined. The spread between the MSC and the interchange fees has narrowed, indicating a high level of pass-through.