

Ingenico / Paymark

Vendor Banks' cross submission on submissions on the Letter of Issues
Counsel-only response to submissions on the Letter of Issues

1. The submissions on the Commission's letter of issues dated 11 July 2018 ("LOI") made by Verifone, Payment Express and Woolworths do not raise any new issues, and largely relate to points on which the Vendor Banks have already made submissions. **Appendix One** includes a table outlining where the Vendor Banks have previously made submissions that address the submissions made by those third parties.

2. In addition, the Vendor Banks make the following additional comments.

The submissions fail to focus on changes resulting from the transaction

3. The third party submissions focus on matters which are of a historic nature and / or wholly unconnected with the transaction (eg whether the Vendor Banks have historically steered cardholders towards S2A transactions, and Verifone's view on the attractiveness of the proposed wholesale / aggregation agreement terms currently on offer). While these are matters on which the Vendor Banks have already responded (see **Appendix One**), they are also not matters which relate to the particular transaction that is the subject of Ingenico's clearance application.

The Vendor Banks' willingness to build links

4. As Payment Express acknowledges in its submission, [] []. To bring some context to this point, [].

5. The fact that Payment Express' current project with [] is not a materially relevant factor in the assessment of the competitive effects of the transaction with the Commission's standard 2 to 3 year timeframe. There are no credible grounds to assert that, within a 2 to 3 year timeframe, Verifone and / or Payment Express will not be able to continue offering switching services for S2I transactions (whether via the continuation of Verifone's aggregation / wholesale arrangements with Paymark; through direct issuer links that have recently been or are currently being established; or through some combination of direct links and access via Paymark's network).

6. Payment Express' suggestion that []¹ does not fit the facts – not least of all that:

- (a) demand for S2A switching services is growing significantly, particularly demand for switching e-commerce transactions;
- (b) Payment Express already has the largest share of online payment gateway services, switching [] e-commerce transactions; and
- (c) Payment Express' submission makes clear that it has built or is actively building STI links (with []) or is in commercial negotiations for building links (with []). On the basis of this evidence, it is likely that Payment Express will have links with about [] Issuers (including the []) in the course of the next 3-5 years.

¹ At [] of its submission on the LOI.

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Payment Express' own conduct and market position is simply inconsistent with its description, for the purposes of its submission to the Commission, of its business as "stagnant".

The attractiveness of a 99% coverage offering to merchants

7. Payment Express is leading the Commission to ask the wrong question when it states that a service that covers 99% of transactions would not be acceptable to merchants.²
8. There is no relevant Factual in which Verifone or Payment Express would be limited to that offering.
9. The correct question is whether the ease with which Verifone / Payment Express can build links and service 99% of transactions provides a credible competitive constraint on the merged entity future conduct. The answer to that question is clearly, 'yes'. That threat has already incentivised Paymark to offer the wholesale terms it has offered to date.
10. As the Vendor Banks have previously submitted, [].
11. Further, by [³]. As a result, after building [] links, including [], the remaining issuers would be mostly loyalty, gift or rewards card issuers (eg MTA cards, Farm Source cards), and other specialist issuers (eg Allied Petroleum or Z Energy fuel cards). These would be the only issuers that would need to be supported via Paymark's links (and, for a number of merchants, such card products may not be relevant in any event – eg switching for fuel cards is really only relevant for the particular fuel company issuing the fuelcard).
12. Payment Express indicated that it would need 9 direct issuer links, in addition to its S2A capability, in order to support a service offering independently of Paymark capable of processing 99% of S2I transactions (para 16). A simple mathematical calculation based on the information provided in its submission is that []. That is plainly a credible threat of bypass that can and will act as a sufficient constraint on Paymark's future conduct in the timeframe that is relevant for the Commission's assessment.
13. Finally, Woolworths' submission is in this respect disingenuous. It comments on what its customers "expect" (a seamless, frictionless, ubiquitous experience). But many Merchants, in their own commercial interests, do not offer that, for example []. While Woolworths plainly sets a high bar for its own customers' experience, the Commission must be careful with a sample of one, not to treat those standards as representative of all customers' actual requirements, or all Merchants' countervailing power.

² At [17] of its submission on the LOI.

³ [].

APPENDIX ONE

Table of cross-referenced responses to Verifone, Payment Express, and Woolworths submissions on the Letter of Issues

Verifone submission			
Submission reference	Submission	Vendor Banks' submission reference	Summary of Vendor Banks' submission
8 - 10	Merchants do not see S2A and S2I transactions as substitutable, because of the differing levels of cost merchants incur.	NERA report at [16] to [28]	Regardless of how the market is defined, Paymark is (and the merged entity will be) subject to competitive pressures in respect of all switching. Pressure will come from a move from S2I to S2A, as well as other pressures (as explained in section 5 of the NERA report).
11	The price differential between S2A and S2I transactions provides the merged entity with a buffer to increase costs of rival switches that rely on access to Paymark's switch for S2I transactions, as well as for Paymark's own S2I customers, without merchants being willing to move to S2A transactions.	Submission on the LOI at [11(a)]	The Vendor Banks are confident that they and merchants can and would steer cardholders to S2A payment types in an effective and timely manner in the face of a post-merger reduction in quality or increase in price of S2I switching services.
		Submission on the LOI at [14], [22] – [23]; NERA report	There are a large quantity of transactions that are either not switched by Paymark, or will not need to be in the near term. There are readily foreseeable developments meaning that there will be pressure on the merged entity to deliver affordable, innovative and relevant switching services, or else by bypassed.
		Cross-submission on the SOPI at [33]	There are a large number of digital payment services that do not currently use Paymark's switch, as well as online and mobile banking products.
13(b)	[].	Submission on the LOI at [19], [29] –[31]	[].
15	The merged entity will have stronger incentives to engage in anticompetitive behaviour in the switching market, as compared to the current incentives – eg restricting access for S2I transactions.	Submission on the LOI at [62]	In order to ensure demand for its switch continues (particularly given the industry drive towards new and innovative payment solutions that do not necessarily require a switching service), the merged entity would be incentivised to foster innovation and competition at the terminal level, rather than foreclosing access to the switch which might otherwise encourage greater

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			utilisation of bypass options and accelerate volume leaving the Paymark network.
16-17, 29	The non-solicitation and volume commitments may create incentives for the Vendor Banks to retain transaction volume on Paymark's switch.	Submission on the LOI at [34] – [41], [57], [59] – [60]; Cross-submission on the SOPI at [3(d)], [37], [40] – [45]	[] []
18	The sale of Paymark to an alternative purchaser is a likely counterfactual.	Submission on the LOI at [42] – [44]	[] The choice of counterfactual is not material to the Commission's analysis, but [].
		Cross-submission on SOPI at [3(a)], [5] – 14]	A Cuscal ownership counterfactual does not reflect commercial reality.
19	Verifone's ability to compete with Paymark is limited to provision of switching services to ANZ-acquired merchants only.	Submission on the LOI at [11(e)], [49] – [55]	It is possible for Verifone and Payment Express to build new links to acquiring banks in order to bypass the Paymark network.
		NERA report at 5.4	Verifone's competitive impact is broader than its ability to compete for ANZ-acquired merchants only.
21	Verifone outlines the difficulties in building new links, including (a) cost (b) need for cooperation and commitment (c) 'collective action' / failure to build problem (d) number of links	Submission on the LOI at [52] – [55]	Verifone's cost estimates of building a new link are overstated, and are more likely to be around [], ie a total cost to build to the 5 issuers of []. In addition, Verifone and Payment Express could split the costs of building the links between themselves, and could piggy-back off each other's links.
		Cross-submission on the SOPI at [19] – [21]	Outline of Verifone's discussions with each of the Vendor Banks about establishing acquirer links.
22 - 25	For high volume merchants, the ability to accept only 99% of transactions would not be acceptable. A loss in large merchants would not be made up for (in volume or value) by a bundle of smaller merchants.	Submission on the LOI at [51]	[]
26, 32(b)	Verifone would need to build links to all, or the vast majority of, the 29 issuers to eliminate reliance on Paymark and effectively constrain the merged entity. [].	Cross-Submission on the SOPI at [3(b)], [16], [18], [21]; Submission on the LOI at [6(b)], [28]	[]. []

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	Building links is a lengthy and difficult process.		
30	Banks are only likely to become aware of anticompetitive conduct after the merged entity had already engaged in a foreclosure strategy. Merchants would need to see price rises, or an inability to accept payments, before exerting competitive pressure on banks.	Submission on the LOI at [11(c)], [25] – [26]	<p>The Vendor Banks' incentives are to offer a variety of terminal and switching services to merchants to meet their customer demand. The Vendor Banks have both the ability and incentive to exercise their countervailing power in combination with the major merchants in this regard.</p> <p>Merchants also have countervailing power, and are not afraid to push back on banks for better (from their perspective) solutions – eg [].</p>
32(a), 43	<p>The means by which the Vendor Banks could respond to a foreclosure strategy are lengthy, meaning that they may be too slow to respond.</p> <p>Direct to account payment methods are unlikely to become sufficiently popular in the next 2 years to materially reduce the number of S2I transactions and the corresponding need to process them.</p>	Submission on the LOI at [14], [70];	<p>There are solutions in-market that do not utilise traditional switch networks, including standard industry API technology. This will also significantly decrease the cost of building links. Minister Faafoi has asked banks to establish in-store versions of electronic bill payment systems within 12 months.</p>
		Cross-submission on the SOPI at [28]	
		NERA report at 5.3.3, 6.3	<p>Three of the Vendor Banks are working with Payments NZ on an API pilot. There are many examples of innovations already occurring in the payments industry – eg ApplePay, ASB's Virtual and ANZ's goMoney wallet. Banks are under pressure to innovate in this space. Innovative technologies mean Paymark is facing an existential threat.</p>
		NERA report at 5.5	<p>The growth of online shopping means that the demand for S2A switching is likely to increase, as virtually all e-commerce transactions are S2A. Further, mobile phone payments may blur the line between e-commerce and POS.</p>
36, 38	<p>Verifone has not received revised offers from Paymark for [].</p> <p>[]</p>	<p>Cross-submission on the SOPI at [25];</p> <p>Submission on the LOI at [11(d)], [45] – [46]</p>	<p>There is no evidence to suggest that the merged entity will not offer the same wholesale terms as the current negotiated terms. []. [].</p>

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<p>37</p>	<p>Verifone cannot be confident that the pricing terms would endure, or that the merged entity would not otherwise frustrate Verifone's access to Paymark's switch, such as [].</p>	<p>Submission on the LOI at [11(d)], [48]</p>	<p>As above.</p> <p>In addition, NERA's analysis indicates that Paymark's business model is highly sensitive to volume loss and, rather than limit access to its switch, it would be incentivised to avoid losing volume to other switches and/or bypass options that are available.</p>
		<p>Cross-submission on the SOPI at [28]</p>	<p>Terminal specifications for connecting to Paymark are effectively set by international standards. [].</p>
<p>39 - 40</p>	<p>The merged entity has an incentive to foreclose rivals in all relevant markets. Paymark's S2I services are an essential input for rival providers of a switching service.</p>	<p>Cross-submission on the SOPI at [29]</p>	<p>Limiting terminal access would be a highly risky and unprofitable strategy.</p>
		<p>NERA report at 6.2</p>	<p>A merchant that wanted to switch away from Paymark for switching services has multiple options, such that the extent of the merged entity's incentive to foreclose is difficult to determine.</p>
		<p>Submission on the LOI at [61] – [62];</p> <p>Cross-submission on SOPI at [30];</p> <p>NERA report</p>	<p>Since the merged entity would be highly sensitive to volume loss, it would stand to lose significant switching revenues if it pursued a foreclosure strategy. The merged entity would be incentivised to foster innovation at the terminal level, rather than foreclosing access to Paymark's switch.</p>
<p>41 - 42</p>	<p>The benefits of the transaction are unlikely to offset the competitive harm of the transaction.</p>	<p>Submission on LOI at [3], [16] – [17], [66] – [68], [71];</p> <p>Cross-submission on SOPI at [35] – [36]</p>	<p>As a global player, Ingenico is best placed to bring global innovation to New Zealand, which will benefit customers, and can compete strongly with Verifone and Payment Express (other vertically integrated businesses). By contrast, [].</p>
		<p>NERA report at 4</p>	<p>Vertical mergers are generally presumed to result in efficiencies, such as the elimination of double marginalisation and pro-competitive bundling.</p> <p>Additionally, Ingenico is likely to have clearer incentives to invest in the competitiveness of EFTPOS.</p>

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44	The merged entity will be able to include emerging payment technologies in any foreclosure strategy, eg by bundling S2I and direct to account services.	Submission on the LOI at [63] – [64]	In most instances, bundling is pro-competitive. The Vendor Banks aim to produce a high quality, attractive offering, and it is ultimately up to merchants what service they want to use.
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Payment Express submission			
Submission reference	Submission	Vendor Banks' submission reference	Summary of Vendor Banks' submission
12	Consumers have been relatively slow to move away from a high level of reliance on traditional EFTPOS payments.	NERA report See also response above in relation to [11] of Verifone's submission	See the NERA report generally, particularly the section on market definition. As noted in Figure 1, [], and as noted in Figure 2, [].
15	In order to compete effectively with Paymark in the S2I sphere, Payment Express would need to establish issuer links with virtually all New Zealand issuers.	See response above in relation to [26] and [32(b)] of Verifone's submission	[]. []
16	Payment Express would need at least <u>9</u> direct issuer links in order to support a service offering capable of processing 99% of S2I transactions (independently of Paymark).	See response above in relation to [26] and [32(b)] of Verifone's submission	As above.
17	Even 99% coverage of S2I transactions by Payment Express would be unacceptable to merchants, who expect ubiquity in terms of EFTPOS acceptance. Payment Express would require at least <u>14</u> direct issuer links in order to offer an acceptable service offering to merchants.	See response above in relation to [22] - [25] of Verifone's submission	[]
20	[]	See the response above in relation to [16] – [17], [19] of Verifone's submission	[] []
24, 25	Payment Express' reliance on Paymark's S2I network will allow the merged entity to raise fees payable by Payment Express, degrade the quality of	See response above in relation to [37], [39] – [40] of Verifone's submission	Paymark is highly sensitive to volume loss, and would therefore be incentivised to encourage terminal innovation, to avoid a loss of volume. Foreclosure would be a risky strategy.

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	its service offerings, or require merchants to use Ingenico terminals if they wish to use Paymark switching services. The merged entity will be incentivised to take these actions.		Terminal specifications for connecting to Paymark are effectively set by international standards.
26	[]	See response above in relation to [44] of Verifone's submission	In most instances, bundling is pro-competitive. The banks aim to produce a high quality, attractive offering, and it is ultimately up to merchants what service they want to use.
		NERA report at [75]	The merged entity would not have an incentive to make it harder for rival terminal suppliers to obtain certification, or harm rivals through bundling or tying, because any of these (or similar) strategies would risk reducing demand for Paymark's switch.

Woolworths submission		
<i>Submission</i>	<i>Vendor Banks' submission reference</i>	<i>Summary of Vendor Banks' submission</i>
The parties claim that it is not necessary to build links to all issuers, but instead only build links constituting 88% coverage is incorrect. The inability to offer a ubiquitous payment experience will be detrimental to retailers. It is unlikely that any retailer would accept such a proposition.	See response above in relation to [22] - [25] of Verifone's submission	[]