COMMERCE COMMISSION – INGENICO/PAYMARK

INGENICO CROSS-SUBMISSION ON RESPONSES TO COMMISSION'S LETTER OF ISSUES

1 Ingenico welcomes this opportunity to comment on parties' submissions to the Commerce Commission's 11 July 2018 letter of issues.

2 This cross-submission is public and does not contain any Ingenico confidential information.

3 Ingenico summarises its key comments below, and provides further specific commentary on the submissions in the *Schedule* to this document.

SUMMARY

—Verifone and Payment Express mischaracterise or overlook the significance of constraints on STI today

4 Verifone's focus on merchants, rather than the banks, overlooks a key dimension of the two-sided payments processing market. This mistaken emphasis on merchant attitudes to payment types, rather than correctly focussing on how the banks view the available payment options, leads Verifone to erroneously state that:

4.1 STI transactions are "largely free" from a merchant's perspective (at [8]) – which is incorrect: each connected merchant pays a monthly access fee to Paymark to ensure it can accept such transactions. Focussing, as Verifone does, on these transactions being largely free to merchants overlooks the commercial reality that the banks meet the bulk of STI switching costs and in aggregate pay a significant amount to Paymark for STI processing capability.

4.2 There is a price differential between STI and STA transactions which the merged entity could somehow exploit (at [11]) – overlooking the reality that there is a price difference in the market today, and would not be altered by the transaction: the proposed transaction does not increase Paymark's ability or incentive to exploit any differential. Ingenico also observes that any such initiative would be likely to (a) accelerate the current trend towards STA, and (b) cause an immediate reaction by the banks, which are presently Paymark's largest customers.

5 Payment Express likewise wrongly assumes that the STI-STA distinction means that merchants would have binary choices when faced with an STI price increase (such as, to have two separate providers and use separate terminals for STI and STA). Payment Express also emphasises that scheme cards are not a direct alternative to EFTPOS functionality (at [9]).

6 Again, Payment Express's analysis overlooks or obscures the true competitive significance of STA: it is another option for the *banks* to offer to their merchant customers. As Ingenico has previously submitted, there is a general shift in market to STA payments in preference to STI, and an accelerating trend towards contactless

payments. These market developments are occurring now and underline the attractiveness of STA and its significance as (one of the) constraints on the STI price. Of course the banks also support STI (proprietary EFTPOS and some scheme debit), reflecting the merchant demand for those processing options too.

7 In summary, STA is presently a readily-available option that most consumers are offered and that most merchants will accept. The proposed transaction will not change the availability of STA as an option. That said, STA's competitive significance in this merger is not as a standalone STI substitute, but as a market feature which reflects customer preferences and enables the banks to—among other things—pressurise Paymark to keep the STI price down.

8 Both the Verifone and Payment Express submissions also overlook the reality that Paymark is constrained in STI switching now – with Verifone (directly) and Payment Express (indirectly) able to use wholesale access to Paymark to offer STI services today. Paymark's recent loss of a major merchant retail chain to a rival (as detailed in previous submissions) demonstrates that those players' STI offering is very real, not just theoretical.

—Payment Express's huge share of digital precludes merged entity from exploiting switching market power to advantage itself in digital

9 Again, Paymark does not have market power in switching services today. That is because Verifone and Payment Express are head-on Paymark competitors. Each has gauged an efficient capital investment strategy and asset mix. Each is winning new merchants at Paymark's expense. The overall result is that Verifone's and Payment Express's pricing offers constrain Paymark all across the market and for all payment types, not just STA. There is also the reality that banks, merchants and consumers are increasingly looking to emerging payment technologies, like the PaymentsNZ Open API pilot, which bypass the switch altogether: these options also constrain Paymark.

10 Verifone's suggestion that the merged entity could exploit its switching assets to benefit itself in digital payments (at [14]) is demonstrably incorrect. The digital payments industry is:

10.1 hotly competitive;

10.2 dominated by Payment Express, with huge share; and

10.3 in Ingenico's experience, characterised by merchants generally separately purchasing digital payments and bricks and mortar POS services.

11 These factors together make it impossible for the merged entity to somehow use its switching market position to advantage itself—or otherwise lessen competition—in digital payments.

—Any Verifone or Payment Express "reliance" on Paymark today is a result of their commercial decisions, not any market features

12 Verifone's self-described "reliance" on Paymark to compete (at [19]) is a product of its own commercial choices since 2012, not any immutable market reality. As the NERA entry analysis shows (and as Paymark's behaviour in the wholesale pricing negotiations underlines), if Paymark was to raise its switching price for STI transactions, Verifone would have a compelling business case for building its own links rather than using Paymark for wholesale access (and could ultimately save money by building its own links). Verifone has nevertheless chosen, no doubt for reasons of commercial self-interest, to use Paymark rather than building its own infrastructure.

13 Verifone's evidence on the difficulty of building links (at [21]) is self-serving. These statements do not align with what Ingenico understands Verifone has said to Paymark about its estimated bypass costs. Given the obvious risks of such evidence, Ingenico suggests that Commission should:

13.1 generally approach Verifone's evidence on this topic with extreme caution; and

13.2 invite Verifone to provide all its internal business records regarding likely link building costs, to ensure the Commission obtains a full picture of Verifone's thinking on link cost and infrastructure investment strategy generally.

14 Verifone's submission also misunderstands or mischaracterises the relevance of the link building threat (particularly at [21] (heading) and [26]). The correct question is whether the threat of link building constrains Paymark's wholesale access pricing now, not whether a standalone Verifone offering might in fact be attractive to merchants. Verifone's speculation about how a fish and chip shop might view a "99% coverage" payment solution is accordingly misdirected, and does not assist the Commission on the core issue of whether Paymark is pricing as if Verifone has a credible bypass alternative. In any event, though, Verifone's factual premise for [24] and [26] is incorrect: Verifone could purchase wholesale access from Paymark and/or Payment Express (which also has some issuer links) to cover the last 1% if necessary.

15 Finally, Ingenico observes that the banks, not Verifone, are best placed to comment on how fast they would react to any switching price increase and what they might do if faced with such an increase: see [31] and [32]. Again, the Commission should treat this evidence with caution and/or disregard it altogether.

16 Again, Ingenico provides further details and detailed commentary on various parties' submissions in the **Schedule**.

SCHEDULE: SPECIFIC INGENICO COMMENTS ON PARTIES' SUBMISSIONS

Para / statement	Ingenico comment
Payment Express (Mullins/Nilsson) letter dated 1 August 2018	

[7] (STI acceptance is a "must have" feature)	Verifone and Payment Express both offer STI switching services to merchants today, enabled by their own links and through Verifone's wholesale agreement with Paymark.
	
	Even if some or most merchants insist on STI functionality, Payment Express overlooks or obscures the constraints on STI today. These will continue post-transaction and mean that the merged entity would not have, and could not exploit, market power for switching services. In particular:
	
	• The shift from STI to STA is clear and accelerating. That trend is driven by, among other factors:
	    o the banks being remunerated through the interchange fee on STA (which they are not for STI); and
	    o contactless transactions (treated as STA) which are attractive to consumers and therefore a feature demanded by large merchants in particular.
	
	• A key result of the trend to STA is that Paymark must invest in STI improvements to keep STI transaction volumes high through better services to merchants, which Ingenico/Paymark wouldn't achieve if it were to somehow foreclose competition.

[9] (scheme cards generally have annual fees and so are unavailable to some consumers)	It's not obvious that EFTPOS card is offered at cheaper cost than scheme debit card. Rather, Ingenico's experience is that many banks offer scheme cards to their customers free of charge or for a notional fee (such as $10/yr), for example: • https://www.bnz.co.nz/personal-banking/everyday-banking/everyday-cards (BNZ Flexi Debit Visa for $10 annual fee, waived in the first year) • https://www.anz.co.nz/personal/accounts/debit-cards/visa-debit-card/ (ANZ Visa Debit Card for $10 p.a., with no charge when linked to an ANZ Freedom or Jumpstart account) • https://www.asb.co.nz/bank-accounts/visa-debit.html?gclid=EAIaIQobChMI6IWS0P_o3AIVg6mWCh3Qlg_BEAAYASAAEgIc9vD_BwE&gclsrc=aw.ds (ASB Visa Debit card, fee $5 per 6 months, no card fees for tertiary or job starter accounts)

Para / statement	Ingenico comment
	• https://www.westpac.co.nz/bank-accounts/debit-cards/debit-mastercard/ (Westpac Debit Mastercard, annual fee of $10, with the annual fee waived for customers on a Career Starter Pac, Tertiary Pac or Graduate Pac) Payment Express's statement is also at odds with para 11 of its submission, which that states that issuers incentivize the use of STA by offering favourable terms to consumers (implying that many customers do enjoy access to "free" or heavily discounted STA cards).
[15] to [17] (issuer links comments and conclusion that significant uncertainties regarding the viability of a "99%" STI service)	Payment Express's comments are incorrect and mischaracterise the current market position. Today, using their own infrastructure and access to Paymark for STI processing under Verifone's wholesale agreement, Verifone and Payment Express (via Verifone) can offer a full service option to merchants. The proposed acquisition of Paymark will not change this existing capability. In any event, though, the presence of STI is best understood as an alternative to STA which is reflective of the banks' preferences, not merchant demands. Paymark, having been established by the banks, enjoys the unique position of having connections to all issuing banks on the domestic market. Its STI offering is, except for the merchant-paid MAF (monthly fee), a cost borne the banks. The banks do today, and will in future, pressurise Paymark to keep its STI fees down, presumably by (in part) underlining the availability of an STA alternative for many transactions.
[27] (merged entity's ability and incentives to foreclose)	The proposed transaction will not change the payments landscape or foreclose any of Paymark's rivals. Once the arrangements contemplated by the sale documents come to an end, the banks will reevaluate their options. The banks will no doubt then insist that Paymark (and others) put forward a credibly competitive offering for all types of payment services. And as Ingenico has explained in detail in its previous (confidential) submissions, wholesale access to Paymark infrastructure will continue to be available post-transaction.
Verifone (Dellow/Manchanda) letter dated 1 August 2018	
[7] to [10] (merchants unlikely to see STA as a substitute for STI/eftpos functionality)	Again, and as stated above in response to the Payment Express letter: • Verifone and Payment Express both offer STI switching services to merchants today, enabled by their own links and through Verifone's wholesale agreement with Paymark. • Even if some or most merchants insist on STI functionality, Verifone overlooks or obscures the constraints on STI today (see Ingenico's

Para / statement	Ingenico comment
	comments above against [7] of the Payment Express letter raising the same points).
[16] (concerns about non-solicitation clause and other provisions assumed to be in SPA)	Ingenico observes that revenue protection mechanisms—such as clawbacks and non-solicitation provisions—are fairly common features of any business acquisitions in any industry. Such arrangements offer a purchaser a degree of protection to, for example, retroactively adjust the price paid against the revenue actually achieved by the business. These protections can be particularly useful where the vendors continue to participate in the relevant industry or sector. Ingenico has previously provided full details to the Commission on the rationale for the proposed transaction terms and the parties' obligations under the confidential sale documents.
[21](a) (link building costs)	Ingenico's experience—detailed in its 3 August 2018 submission—is that link building costs are far lower than the $500k to $1m figure cited by Verifone here. Banks in some cases sponsor or part-pay for link-building investment. Moreover, Verifone's statements do not align with what Ingenico understands Verifone has said to Paymark in the wholesale negotiations about its estimated bypass costs. Given the obvious risks of relying on such statements, Ingenico suggests that Commission should generally approach Verifone's evidence on this topic with scepticism.
[22] to [24]	Verifone's speculation about how a fish and chip shop might view a "99% coverage" payment solution is misconceived and does not assist: o The correct question is whether Paymark's pricing is constrained by the possibility of Verifone developing a bypass alternative, not whether a hypothetical "99%" offering might or might not be attractive to a given merchant. o In any event, though, Verifone's factual premise for [24] is incorrect: Verifone could purchase wholesale access from Paymark (which has a full set of issuer links) and/or Payment Express (which Ingenico understands also has some links) to cover the last 1% if necessary.