23 JULY 2024

Retail Payment System

Costs to businesses and consumers of card payments in Aotearoa New Zealand: Consultation Paper

Submission Template

Purpose of this template

1.1 This template provides details on how to make submissions on our **Costs to businesses and consumers of card payments in Aotearoa New Zealand: Consultation Paper** and the confidentiality considerations.[1] It also provides the full list of questions outlined in the paper to assist with written submissions.

Providing your views by submission

1.2 We are seeking your feedback on the views and questions raised in our paper, and on any other aspects of the retail payment system landscape that you consider relevant. Your feedback will help inform whether a review of interchange fee regulation is necessary.

1.3 In addition to written submissions using the process set out in this document, we also welcome requests to meet to discuss any aspects of this paper (within the consultation period) and are open to conducting facilitated feedback sessions with stakeholder groups. Please contact us if you think either of these alternative engagement options would be beneficial.

1.4 You do not need to respond to all the questions raised in this paper, you can instead just respond to the questions that relate to your business operations or experience.

1.5 Whilst we will accept a range of formats, our preference is for submitters to use this template. Responses can be emailed to RetailPaymentSystem@comcom.govt.nz with 'Consultation on costs to businesses and consumers of card payments in Aotearoa New Zealand' in the subject line.

1.6 To ensure your feedback can be considered, please provide this to us by **4.00pm, Tuesday 20 August 2024**.

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[1] Commerce Commission "Costs to businesses and consumers of card payments in Aotearoa, New Zealand: Consultation Paper" (23 July 2024) available at https://comcom.govt.nz/regulated-industries/retail-payment-system#projecttab

Confidentiality

1.7 While we intend to publish submissions on our website, we understand that it is important to parties that confidential, commercially sensitive, or personal information (confidential information) is not disclosed as disclosure could cause harm to the provider of the information or a third party.

1.8 Where your submission includes confidential information, we request that you provide us with a confidential and a public version of your submission. We propose publishing the public versions of submissions on our website. We note that responsibility for ensuring that confidential information is not included in a public version rest with the party providing the submission.

1.9 Where confidential information is included in submissions:

1.9.1 the information should be clearly marked and highlighted in yellow; and

1.9.2 both confidential and public versions of submissions should be provided by the due date.

1.10 All information we receive is subject to the principle of availability under the Official Information Act 1982 (OIA). There are several reasons that the Commission may withhold information requested under the OIA from disclosure. This includes, most relevantly, where:

1.10.1 release would unreasonably prejudice the commercial position of the supplier or subject of the information;

1.10.2 withholding the information is necessary to protect the privacy of natural persons; and

1.10.3 we received the information under an obligation of confidence, and if we were to make that information available it would prejudice the supply of similar information to us (by any person) where it is in the public interest that such information continues to be supplied to us.

1.11 If we consider that any of these potential reasons for withholding apply, we must still consider the public interest in release. As the principle of availability applies, the information may only be withheld if the potential harm from releasing it is greater than the public interest in disclosure. This ‘balancing exercise’ means that in some cases information can be released where nonetheless there is some possible harmful effect that might appear to justify withholding it.

1.12 We do not need to receive an OIA request for information for the principle of availability to apply. We can release information that in our assessment should be made publicly available. We will not disclose any confidential or commercially sensitive information in a media statement or public report, unless there is a countervailing public interest in doing so in a particular case. Such cases are likely to be rare.

1.13 We will consider any request from a party who wishes to keep their identity and/or the content of their submission anonymous. However, this request must be discussed with us first before the submission is provided to us. Submitters must justify any request for anonymity by providing reasons.

1.14 **Table 1.1** provides the full list of our submission questions.

Table 2.1 **Full list of our submission questions**

<table>
<tr><th>Question number</th><th>Target Audience</th><th>Question</th></tr>
<tr><td>1</td><td>Merchants</td><td>Do merchant service fee complexities drive challenges in determining whether and how you surcharge?</td></tr>
<tr><td>2</td><td>Merchants</td><td>Would you consider lowering or even ceasing to surcharge if your merchant service fees were less than 1% for in person card payments?</td></tr>
<tr><td>3</td><td>All stakeholders</td><td>Is token portability an issue in New Zealand? If yes, what is stopping the implementation of the Reserve Bank of Australia’s expectations here?</td></tr>
<tr><td colspan="3">For Revolut in New Zealand, token portability is not an issue. However, we do support the implementation as token portability empowers the customer to manage payment information more easily, securely, and flexibly across different platforms and services.

Token portability is expected to enhance consumer choice and promote competition among payment service providers. If consumers can easily switch providers, it forces companies to compete more on service quality, pricing, and features, which ultimately benefits consumers. This will also reduce the exposure to Fraud as a secure tokenised version of the card is saved across platforms rather than the card details.

Apart from creating competition, Token Portability also benefits Merchants & Service providers as it reduces the risk of losing customers who might otherwise be reluctant to switch providers due to the inconvenience of having to update their payment credentials across various platforms.</td></tr>
<tr><td>4</td><td>All stakeholders</td><td>We welcome further evidence of any other issues within the New Zealand retail payment system</td></tr>
</table>

Terminal selection

Revolut Payments New Zealand Pty Ltd (RPNZ) operates within the New Zealand payments system via international scheme rails. Therefore, when selecting the type of account at the terminal, although using a prepaid card the customer needs to select 'Credit' otherwise the payment will fail. We understand that this is due to the fact that if Debit is selected, the payment transaction attempts to switch via EFTPOS, of which we are not a member. This is a flaw in the payments system for fintechs similar to Revolut who use prepaid cards, as there is reliance on customer education.

[redacted]

[redacted]

[redacted]

[redacted]

Cost to merchants

The charge to merchants comprises four costs:

1. Interchange (A cost paid by the acquirer to the issuer)
2. Scheme Acquirer Fee (A cost charged to the acquirer by the International Scheme)
3. Acquirer margin
4. Terminal fees/rental [Card Present only]

A reduction in interchange typically only helps the largest merchants, on "IC++" contracts with their acquirer. This means their costs are disaggregated, with a breakdown in the costs provided to the merchant. If Interchange reduces, these merchants would see a reduction in the fees that they pay to their acquirer. As such, they may also reduce the surcharge - but critically, we do not believe they would be required to do so.

[redacted]

Cost to issuers

The cost to issuers includes:

- Negative Balance /Overdraws
- Issuing Chargebacks / Fraud
  - Unauthorised Card Fraud
  - Authorised Card Fraud

Question number	Target Audience	Question
○ Disputes ○ Collections ● Scheme Fees ● Processing Costs Please let us know if you would like further information on the above costs. <u>Surcharging</u> Following the designation of Mastercard and Visa in 2022 and following initial caps, there has been no change to surcharging regulation or reduction incentives. We have therefore seen limited change to surcharges and subsequently few benefits from the reduction in interchange have been passed to the customer. Therefore we would propose a review of surcharging prior to any interchange fee reviews which have only recently been reviewed. Merchant acquirers in New Zealand offer bundled and unbundled /IC++ pricing options. Under bundled pricing, merchant service fee is fixed and includes all acquiring fees and a fixed interchange fee that is the average of all the possible interchange fees on different card types - from contactless domestic debit, to international credit. Comparatively, under unbundled pricing merchants pay the correct price per transaction (i.e. the exact interchange fee for each transaction plus the fixed acquirer fee). As interchange fees vary depending on many factors, unbundled can often be cheaper for merchants. Therefore, when interchange reduces, these merchants would see a reduction in the fees that they pay to their acquirer and as a result are more likely to also reduce the surcharge. However, in New Zealand we have seen evidence that many merchants are still on bundled rates, as pricing is easier to understand. We believe this to be quite unique to New Zealand compared to other markets, such as Europe and North America where unbundled pricing is the preferred pricing option. It is our belief that the wide usage of bundled pricing by New Zealand merchants is one of the key reasons that benefits from the initial interchange caps were not passed to customers. Therefore encouraging surcharging reduction would encourage unbundled pricing.		
5	Schemes, Issuers, Acquirers	What do you consider an appropriate methodology for determining interchange fee caps in New Zealand? Why do you think this best meets the purpose of the Retail Payment System Act, and how would it be practically implemented?
6	Schemes, Issuers, Acquirers	What is the rationale for the heavy discounting of interchange fees to large businesses and the evidence to support the extent of the discounting observed?
7	**Mastercard, Visa, Issuers**	**What evidence is there to support higher interchange fee rates for credit versus debit card payments?**

Question number	Target Audience	Question
More value to Merchants The increased spending capacity of credit card users can lead to higher transaction volumes, making them more valuable customers than those using debit cards. The higher interchange fees can be justified by the increased value they bring to merchants and the increased costs that issuers face enabling these cards for customers. An alternative spending method gaining popularity in the market is Buy Now, Pay Later (BNPL) services. According to MBIE, 80% of surveyed consumers used BNPL in the past year, with nearly half using it fortnightly. Merchants utilising BNPL services face significantly higher merchant service fees (typically at least 4%) compared to Visa/Mastercard (currently between 1.5-2%). However, the widespread adoption of BNPL despite these higher fees indicates that merchants perceive substantial value and benefits in credit spending behaviour because customers are able to spread the cost, particularly with higher value transactions with another party (other than the merchant) taking the associated credit risk. This shows that merchants are willing to accept higher fees to leverage the advantages of increased consumer spending power. Increased risk Credit card transactions involve a higher level of risk for issuing banks compared to debit card transactions (e.g. fraud and chargeback costs). More robust risk management practices are required to manage this elevated level of risk. If interchange fees are lowered, credit products may become less diverse or readily available. This will in turn put pressure upon merchants to provide their own credit facilities to support their business.		
8	**Mastercard, Visa, Issuers**	**We welcome quantitative evidence justifying higher interchange rates on domestic card not present transactions.**
While Card Not Present (CNP) transactions offer a convenient means for customers to be able to pay for online goods and services, that convenience does come at a cost. Advanced security measures CNP transactions are supported by advanced authentication and security technologies, such as 3D Secure (3DS) and other two-factor authentication (2FA) measures. While these technologies are essential for mitigating fraud, they come at a considerable expense, resulting in processing costs that are notably higher than those for Card Present (CP) transactions. Fraud detection and prevention In Australia, CNP fraud accounted for 90% of all card fraud in 2022 (based on a report published by AusPayNet). This highlights the significant risk and associated costs involved with these types of transactions. As technology and methods of CNP fraud evolve, so too do the requirements for sophisticated fraud detection and prevention systems. Significant costs and investments are required to constantly develop and upkeep internal fraud detection capabilities. Chargebacks An important consumer benefit for using a Visa/Mastercard is the chargeback feature. This gives consumers an additional layer of protection against fraudulent or disputed transactions. This chargeback process raises the overall system cost through administrative overhead and potential losses.		
9	Mastercard, Visa	We are seeking evidence on the rationale and methodology used to set the difference between interchange fee rates on cards issued within New Zealand and foreign issued cards.
10	Mastercard, Visa	Why are two categories of rates for foreign-issued cards (inter-regional and intra-regional) necessary?
11	**Mastercard, Visa, Issuers, Acquirers**	**Who is liable for the fraud costs associated with transactions made using a foreign-issued card?**

Question number	Target Audience	Question
The liability for fraud costs associated with transactions made using a foreign-issed card typically depends on several factors, including the type of transaction and the technology used by the merchant. For CNP transactions, liability shifts from merchant to issuer when verification technology such as Face/Touch ID (XPay) or 3DS (ecommerce) is used to verify the transaction. For CP transactions, liability generally shifts from merchant to the issuer if the merchant's terminal is equipped with EMV chip technology and the customer enters a PIN to authenticate the transaction. However, for contactless payments, no PIN is required at the terminal if the transaction amount is under the cap set by the issuer (usually $100). In these instances, there will be no liability shift and the merchants would absorb the cost. The above rules are governed by Visa/Mastercard's EMV Liability Shift rules and are consistent throughout the APAC region for all domestic, intra-regional and inter-regional transactions.		
12	Mastercard, Visa, Issuers, Acquirers	We are seeking quantitative evidence of differences between levels of fraud for domestic and foreign-issued cards.
13	Mastercard, Visa, Acquirers	We welcome evidence and rationale for why merchants are treated differently for interchange fee application.
14	**Mastercard, Visa, Acquirers, Issuers**	**We welcome evidence of the impact of hard caps and percentage rates on compliance costs.**
Response combined below with answer to Q15.		
15	**Mastercard, Visa, Acquirers, Issuers**	**Please provide evidence of any other aspects of the implementation of any changes to interchange fee caps that impacts compliance or other business costs.**
Implementation of weighted average interchange fees, similar to the approach taken in AU, would primarily affect the compliance and monitoring responsibilities of the card schemes who determine the interchange fees (i.e. Visa and Mastercard). These card schemes would need to continuously monitor transaction volumes, and recalibrate as necessary, to ensure the weighted average does not exceed the caps. However, this approach is far better for business and innovation, as it allows for different rates to be set based on different product characteristics. Conversely, compliance with hard cap interchange fees is more straightforward. However, this simplicity would come at the cost of reduced flexibility. Card issuers would have fewer incentives to offer a diverse range of products, as they would not be appropriately compensated for the varying costs and risks associated with different offerings. If interchange fee caps are changed, the key impact for RPNZ would be on monitoring revenue and forecasting future earnings. On the compliance side, RPNZ currently relies on the card schemes to apply interchange fees accurately, and we do not reconcile or verify the fees ourselves.		
16	Acquirers	How would you reduce merchant service fee rates for your customers on fixed or blended pricing?
17	Acquirers	How would you provide your customers with an overview of the intended impact on them of further price regulation?
18	Mastercard, Visa, Issuers, Acquirers	How fit for purpose is the current anti-avoidance provision? Please provide evidence of any challenges and whether there are other more efficient solutions.
19	**All stakeholders**	**Please provide any evidence of other impacts a material reduction in interchange fees for Mastercard and Visa could have on the New Zealand retail payment system.**

Question number	Target Audience	Question

A material reduction in interchange fees for Mastercard and Visa could have several detrimental impacts for the New Zealand retail payment system.

[redacted]

Decreased funding for customer fraud protection
RPNZ allocates a significant portion of funds to the development of financial crime prevention capabilities and consumer protection measures. If total revenue would not cover these fincrime costs, it would either become unviable to continue operations, or these costs would need to be recovered through other means, such as alternative fees.

Reduction of product benefits
A material reduction of interchange fees would also adversely impact the consumer benefits associated with card products, such as complimentary insurance, fraud protection and aforementioned reduction in innovation and tech improvements.

Unintended consequences of domestic fee regulation
We believe that there could be a “waterbed” effect to reduction of interchange fees. This means that a reduction in interchange fees could mean that fees increase in other areas, leading to a net-same Merchant Service Charge or customer surcharge. It is worth us reiterating that the Merchant Service Charge comprises a number of cost items that are passed on by the acquirer. Therefore we would not be confident that a reduction in interchange will ultimately reduce costs of card payments to consumers or businesses.

Merchant Indifference Test
Revolut has previously been a part of long term Merchant Indifference Tests in other jurisdictions where there have been proposals to change interchange fees. This has been a successful way of calculating the appropriate interchange objectively in the market and Revolut would be willing to support testing in New Zealand.