

American Express response to consultation on Article 19 and Article 22 of Directive 2011/83/EU on Consumer Rights

American Express welcomes the opportunity to respond to the Irish Government's consultation on Article 19 (Fees for the use of a means of Payment) and Article 22 (Additional Payments) of Directive 2011/83/EU on Consumer Rights (CRD).

Rather than respond to each question in turn we set out the key material general points which we wish to represent to the Government, as follows:

- (a) While we support the overall aim of the Government's proposals to tackle the harm associated with excessive surcharging practices, we believe the proposals to cap surcharges at cost enshrined in Article 19 in particular do not go far enough to address consumer harm in this area. We therefore urge the Government to consider prohibiting surcharging practices altogether in the best interests of consumers, as it is permitted to do under the Payment Services Directive (PSD).
- (b) If — notwithstanding these concerns - the Government proceeds with the current proposals, we note that:
 - "Cost" evaluation is complex to apply, monitor and enforce, and therefore that any new regulatory requirements and guidance should not be unduly prescriptive; and
 - Concepts of "payment type" should be considered broadly and pragmatically (e.g. (i) debit cards (ii) credit and charge cards. (iii) e-wallet etc) as there is no basis for treating these products differently.

We address each of these points in more detail as set out below:

(a) Current proposals are inadequate to address consumer harm — instead surcharging practices should be prohibited altogether in the interests of consumers:

While we support the overall aim of the Government's proposals to tackle the harm associated with excessive surcharging practices, we believe the proposals put forward do not go far enough. Fundamentally, we do not agree that the consumer's interests are best served by allowing merchants to surcharge consumers for what is only one element of their cost of doing business. We note in this connection that the Irish Government has itself observed that *"Though consumers may benefit from reduced prices in some instances, it is more realistic to expect that the total price to the consumer will*

*not fall in most cases*¹. In addition, it notes that surcharges have the effect of lowering the headline price of goods or services thereby distorting purchasing decisions in ways that likely result in consumer detriment². This view is also supported by the UK Government's impact assessment in connection with its concurrent consultation on the implementation of the CRD, which concludes that whilst all the measures it considers to restrict surcharging, including an outright ban on surcharging, are price neutral from a merchant's perspective (since either a merchant does not surcharge currently, or they will adjust the headline prices or additional fees to compensate), from a consumer's perspective the benefits of an outright ban are extensive. The assessment states (*inter alia*):

"Consumers will no longer be misled by unavoidable payment charges that are separate from the headline prices. This will support efforts by the Government to make prices and charges transparent at the outset of a transaction, rather than being built up in stages as a transaction progresses. This "drip pricing" practice is assessed as having the main potential to mislead customers..."

No matter which payment method used, consumers will be able to compare prices and shop around more easily. Better price comparability will enhance competition, particularly in the transport sector where payment surcharges are most prevalent. This will have wider benefits, in terms of facilitating e-commerce.

Consumers who avoided paying by credit card because of a higher surcharge imposed will be enabled to switch to another payment method without any additional fee charged by the merchant.

The prices will be easier to understand as there won't be any differences according to the payment method chosen. This will benefit especially those customers who aren't able to differentiate between a debit and a credit card.³"

The PSD very clearly gives Member States a choice as to whether to permit or prohibit surcharging and this is not superseded by the requirement to consider implementation of the CRD. The very fact that the European Commission, in its recent Green Paper issued post-CRD, is querying whether the PSD should be amended to achieve full harmonization on surcharging

¹Consultation on Article 19 (Fees for the use of a means of Payment) and Article 22 (Additional Payments) of Directive 2011/83/EU on Consumer Rights, paragraph 11.

²Consultation on Article 19 (Fees for the use of a means of Payment) and Article 22 (Additional Payments) of Directive 2011/83/EU on Consumer Rights, paragraph 3.

³UK Government, BIS Consultation on the early implementation of a ban on above cost payment surcharges: Impact Assessment, page 29.

rules across the EU further suggests that Member State options around surcharging under the current PSD remain intact post-CRD.

American Express strongly believes that banning surcharging is the only adequate remedy to prevent the exploitation of consumers. We note that, during the implementation of the PSD, the Consumers' Association of Ireland took a strongly anti-surcharging position. More recently, in the U.K., both the consumer body *Which?* and the Office of Fair Trading conducted consumer research that confirm that the vast majority of consumers object to the imposition of extra charges simply for paying with a card, i.e., paying to pay.⁴ If such a ban were imposed, merchants would still remain free to discount for certain payment instruments, such as cash, should they wish to do so.

Many jurisdictions follow this approach and yet, few merchants choose to apply any discount. In our view, this further demonstrates that there is no real intent on the part of merchants to pass any benefit onto consumers to encourage them to pay using a supposedly lower cost payment option⁵.

Surcharging allows a merchant to pass on all the costs of accepting payments, without any corresponding benefit being provided to the consumer. The value of a card payment to the merchant is considerable and includes the payment guarantee, prompt and efficient payment, processing services, marketing and rewards programmes and the wider social benefits associated with electronic payments. With the ability to surcharge merchants have effectively been given the opportunity to 'free ride' the system on the backs of their customers.

In the case of American Express, in particular, in order to remain a viable competitive alternative to the dominant payment schemes of Visa and MasterCard, we make substantial ongoing investments to increase the value of card acceptance to merchants. This value goes beyond the pure mechanics of the card acceptance process and extends to our ability to bring together buyers and sellers through our unique ability to connect card holders directly with merchants via our closed loop network. We invest heavily because we understand American Express card acceptance is a choice for merchants. All of these pro-competitive actions are completely undermined by the blunt instrument of surcharging.

⁴80 per cent of members of the public surveyed by *Which?* stated that there should be no additional fees for paying by card and only 5 per cent agreed that there should be additional fees for paying by card (*Which?* Super-complaint, section 3.1.1, page 56, and section 3.4, page 89 onwards). The OFT's consumer research found that 87 per cent of consumers objected to extra charges for credit cards and 91 per cent objected to extra charges for debit cards (OFT Response to Super-Complaint, citing OFT 2010 study 'Advertising of Prices Market Study www.of.gov.uk/OFTwork/market-research/completed/advertising-prices/).

For example, a recent study conducted by the Electronic Payments Coalition in the United States, and published on 28 September 2012, of the prices of identical products sold at several U.S. retailers before and after debit interchange was reduced by U.S. Federal Reserve Board regulation (the 'Durbin amendment') by at least 40 % showed virtually no reduction in prices to consumers, despite the substantial reduction in interchange experienced by merchants. To the contrary, in most instances, prices increased.

Many of the incidents of excessive surcharging identified to date have taken place in the online environment, where customers are effectively "trapped" with only limited payment options that do not attract a surcharge. For customers to suffer surcharges in such an environment, with no corresponding price reductions being offered to them as a result of online sales being less costly than bricks and mortar retail sales (i.e., lower staffing & real estate costs) serves to demonstrate how this captive online audience is being exploited, and exposes the real intent behind surcharging practices — to generate additional revenue.

Moreover, in our view there is no legitimate reason why the costs of card acceptance should be singled out in this way as compared to other costs of doing business.

In conclusion, a decisive prohibition on surcharging would comprehensively address all the anti-consumer issues associated with surcharging practices. Importantly, there is significant support for such an approach across Europe. Indeed, we note that a number of Member States (Austria, France, Greece, Hungary, Italy, Latvia, Lithuania, Romania, Sweden and Slovakia) have taken this approach pursuant to the PSD Article 52(3) in the interests of promoting efficient electronic payment methods. More efficient payment methods, including credit and charge cards, are less costly to the merchant and to society than cash. By not considering the option to prohibit surcharging entirely, the Government risks missing the best and most direct opportunity to protect consumers. We therefore recommend that the Government should exercise its policy discretion under the PSD to prohibit surcharging for all payment transactions in order to prevent ongoing consumer detriment.

(b) "Cost" evaluation is complex to apply, monitor and enforce, therefore regulations should not be unduly prescriptive and guidance should be broadly drawn

Our responses which follow are made on the assumption that the Government is not minded to reopen the basic question of whether or not to ban surcharging and intends to proceed as outlined in the consultation document. Our responses should be read in this light, and do not suggest that American Express agrees that surcharging is in the interests of the consumer.

We agree with the Government's proposal to adopt the Articles in the Directive as worded and that regulations should not be prescriptive given the complexity and wide variances involved. The guidance documents will therefore be key to interpretation of the legislation.

The concept of 'cost' in this context is not straightforward and cannot easily be measured (either across (i) debit payments (ii) credit and charge card payments (iii) e-wallet payments or between these and other forms of

payment). Moreover, there have been hundreds of economic surveys done on this subject with no clear conclusions. Widely different commercial terms are agreed between merchants and their acquirers and which can vary by card type, volume and other measures. As such, we consider that it is virtually impossible for any merchant to determine the true cost of accepting a particular card payment for a particular transaction.

We note that the pricing constructs for the dominant schemes have become increasingly opaque in recent years as they have come under more and more scrutiny. This has served to create even less transparency in the system. By contrast, American Express has always had, and continues to have a very simple pricing model, but one which represents a broader relationship value to merchants going far beyond the pure mechanics of payment.

We would also note that costs paid have to be measured against value received. Yet, this is a highly fact-specific assessment that is not possible to define within the scope of a broad brush regulation.

If the Government remains committed to implementing some form of cost limitation on surcharging requirements, we consider it vital that at a minimum all the costs identified in the consultation document are included within the guidance issued to merchants outlining the costs they can take into account when assessing levels of surcharge.

However, American Express also suggests that other key areas need to be factored in to better understand these 'costs', and the complexities that are associated with their assessment:

- First, the Government cites the largest component of merchant fees as merchant service charges ("MSC"), and that it is possible to gain an insight into the level of such fees from Multilateral Interchange Fees ("MIF") applied by the dominant card schemes of Visa and MasterCard. This assertion by itself is inaccurate, since the smaller, three-party schemes such as American Express have no MIF, as they contract directly with merchants for acceptance of American Express-branded cards in the UK, and consequently apply a completely different and much broader value assessment when agreeing fees with merchants.
- Second, the relationship between merchants and acquirers for the dominant must-carry payment schemes is frequently characterised by additional fees and costs dependent on the card accepted, which routinely act to raise the cost of card acceptance, over and above the headline "MSC" cost. In the U.K., the OFT's Response to the *Which?* super-complaint acknowledged in its analysis these additional costs in

involved in the dominant schemes⁶. The impact of these fees is significant, and makes any attempt at a comparable assessment of the 'cost' of acceptance inherently challenging. Some merchants will face more of these fees than others, meaning that the rate per transaction can vary widely and render it virtually impossible to assess. This practice is in contrast to American Express as: firstly, American Express acceptance is a genuine choice; secondly, each merchant pays a single individual rate in any given agreement with a merchant regardless of which American Express-branded card has been accepted (known as the "Discount Rate")

- Third, it is incorrect to characterise the Discount Rate in the American Express system as merely a 'cost' of card acceptance without considering a range of additional factors that contribute to the broader value we bring to merchants who accept the American Express card. Other components of value include higher average charge amounts and higher frequency of use on American Express-branded cards driven by our affluent and loyal global cardmember base. On top of providing merchants the potential for incremental sales, we also provide valuable information and fraud services, marketing opportunities and other support to merchants through a dedicated client management organisation. In addition, a merchant's Discount Rate is influenced, among other factors, by the merchant's charge volume, the method of submission of payments to American Express, the speed of pay

This means that the whole cost/value exchange between American Express and its merchants not only extends beyond

⁶ OFT Response to *Which?* Super-Complaint, paragraph C4.

the pure mechanics of card acceptance but is extremely dynamic as well, responding to both merchant and cardmember needs.

- Fourth, for many bank acquirers the acquiring arrangement with a merchant is just one small element of a much larger banking relationship. A bank acquirer on the Visa or MasterCard networks may price card acceptance taking its entire banking relationship with a merchant into account. This may include fee or interest income from the merchant for secured and unsecured business loans, investments, current account operation, trade finance or factoring, foreign exchange services and other services. This provides significant scope for cross subsidies and trade-offs, which may result in merchant acquiring services being provided with misleading price signals. The potential for cross subsidisation across a broader range of banking and financial services clearly provides the opportunity for the costs of card acceptance to be shifted to other revenue streams between the merchant and the bank, rendering it impossible for any merchant to make a true assessment of its costs.

Therefore, while we acknowledge there is some recognition in the Government's proposals that evaluating the true cost of merchant acceptance is complex, we remain concerned that the consideration given in the consultation document of cost categories does not provide the full picture and should be expanded if the cost-based approach is mandated.

Accordingly merchants ought to be obliged by any guidance issued to consider the following relevant factors to the cost of card acceptance:

- a. Other costs payable to acquirers. This cost category includes: fees for the rental and maintenance of payment card terminals; scheme fees incurred in processing card payments and levied by the acquirer (e.g., international service assessments or cross-border transaction fees); and other fixed fees for providing payment acquiring equipment and services (e.g., other monthly or annual fees that are included on the merchant's card processing statement).
- b. Costs payable to other payment service providers. This cost category includes: gateway fees; switching fees; and fees for the provision of equipment and/or services required to accept card payments.
- c. Merchants' own costs related to card acceptance. This cost category includes: the merchant's costs of purchasing and maintaining their own card acceptance infrastructure; scheme fees levied on the merchant by

the scheme; and line rental and communications charges directly related to the use of payment card terminals.

- d. Fraud costs related to card acceptance. This cost category includes: the transaction value of fraud-related chargebacks; chargeback fees charged by the acquirer or a payment service provider; and any fixed equipment, systems or development costs that are incurred by the merchant as a direct result of compliance with scheme rules or mandated requirements.
- e. Any fixed equipment, systems or development costs, not already captured in paragraphs (a) to (d), that are incurred by the merchant as a result of compliance with scheme rules or mandated requirements or standards.
- f. Costs related to data security. Merchants face costs ensuring that they meet and adhere to the current industry standards in respect of processing and managing sensitive data that could be subject to either loss or malicious attack (e.g., the PCI Standard).

Importantly, care should be taken to ensure that any requirements or guidance are not drafted too prescriptively, recognising the wide variances we have referred to above_

In any case, ultimately, the imposition of limits on surcharging only tinker with what remains in our view a fundamentally flawed policy of giving merchants the right to surcharge.

We consider it appropriate that CRD implementing guidance should enable merchants to assess their total costs across all payment types (e.g. (i) debit, (ii) credit and charge, (iii) e-wallet, etc.) and that the guidance to merchants should be to limit their surcharges accordingly.

About American Express

While remaining small in scale compared with the four-party schemes, American Express operates probably one of the best-known proprietary three-party card schemes worldwide. Our three-party scheme is proprietary because American Express itself operates the network and typically acts as both issuer and acquirer, in contrast with the four-party schemes of Visa and MasterCard, neither of which issues cards or acquires transactions. Most notably, there are no multilateral interchange fees in the American Express scheme. Instead, American Express's merchant fees (referred to as discount rates) are negotiated bilaterally and directly with merchants. As such, merchants therefore have a clear choice whether or not to accept American Express cards. Merchants that do not consider American Express delivers

value for money are free not to accept American Express cards, and there are many examples of such merchants.

In order to expand its business more quickly and effectively, American Express has established licensing relationships with approximately 120 partners worldwide, including in Ireland, where we have partnered with Elavon, which provides merchant acquiring services.

The American Express licensing business is not constructed or managed in any way like a four-party card scheme. Critically, unlike the Visa and MasterCard model, all of our licensing arrangements are bilateral and confidential; we do not operate as an association and there are no links or undertakings between licensee partners. Specifically, there are no relationships between the partners: and there is no collective decision-making on fees or scheme rules. Our licensee partners have no equity interest, nor do they have any role in governance or decision-making at any level. Furthermore, our partners have no involvement in deciding who may qualify for an American Express licence. The licensee's sole relationship is with American Express and is strictly contractual, pursuant to a bilateral and confidentially negotiated agreement between the licensee and American Express.

American Express makes substantial ongoing investments to operate a competitive card network from end to end, including: operations, service delivery, systems, authorisation, clearing, settlement, dispute resolution, fraud prevention, certification of third party service providers, rewards programmes, brand advertising and marketing, new product development, rewards and other cardholder and merchant benefits, and establishing and enhancing relationships with merchants, cardholders and issuing and acquiring partners globally. Many of these investments directly benefit merchants who accept American Express cards, effectively driving considerable value to our merchants.

For example, the American Express business model provides us with a "closed loop" of transaction information which enables us to have deeper knowledge of card spending on our network and to develop targeted marketing programmes and benefits that attract and retain high-spending, loyal customers to carry and use American Express cards globally and encourage them to spend at merchants who accept the American Express Card. The "closed loop" is widely recognised as a distinctive and competitive characteristic of the American Express card network. Cardholders and merchants who recognise the value created by investment in these programmes and benefits are willing to pay a price commensurate with the value they receive from such investments. Merchants do not have to accept American Express to operate their business, as they may consider to be the case for our competitor four-party schemes. We constantly have to reinforce

and prove our value to cardholders and merchants alike and we face strong competition from the dominant duopoly of Visa and MasterCard.

Unlike the 'must carry' networks of Visa and MasterCard, American Express is a genuine choice. Many consumers choose not to carry American Express cards (and the vast majority who do also carry other payment products, including other credit and debit cards); and merchants do not have to accept American Express. Indeed, many merchants have chosen not to do so [REDACTED] [REDACTED]. To compete effectively, American Express has built a business model on brand differentiation, focusing on delivering premium value.

For the reasons outlined above American Express remains convinced that the argument for banning surcharging altogether is more compelling than ever and that the Government should consider this afresh in the light of the discretion it is given under the PSD and in light of the trends we see in a number of EU countries.

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