EurActiv.com
EU News & Policy Debates

SPECIAL REPORT | 8 - 12 July 2013

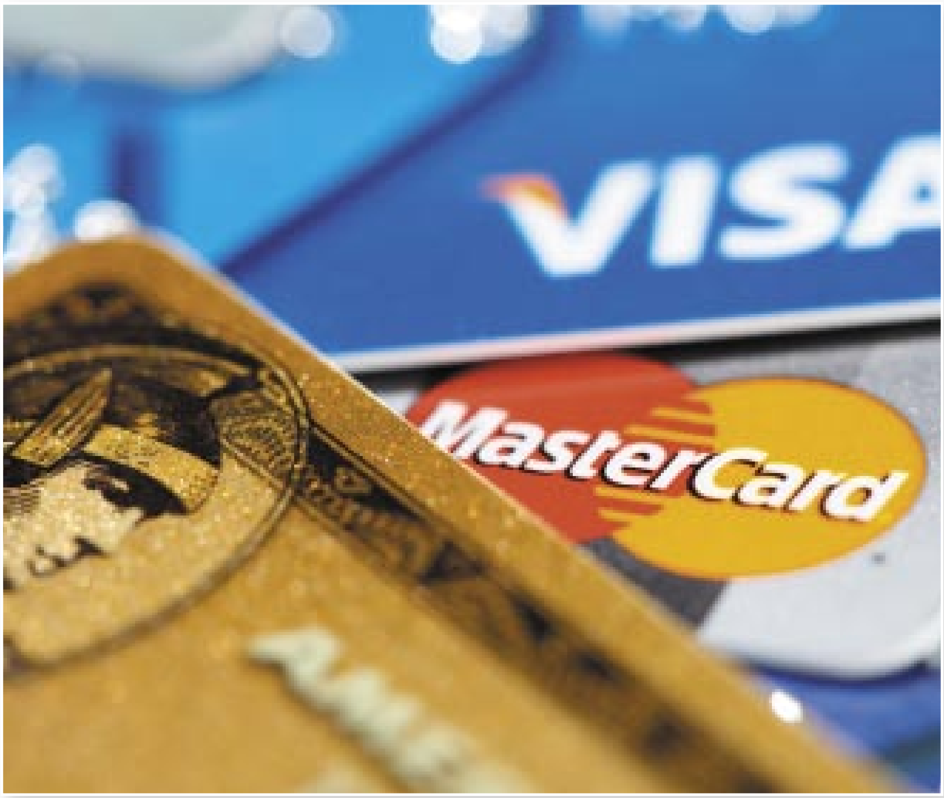
With the support of MasterCard

PAYMENTS SERVICES DIRECTIVE II

http://www.euractiv.com/special-report-payments-services-directive-2

Contents

EU's new payments directive to cap fees, ignite consumer debate



Forthcoming European Commission proposals that are aimed at levelling the playing field for payment cards across Europe are likely to ignite disputes over new market entrants and consumer benefits.

The Commission is set to publish its update to the Payment Services Directive (PSD II) this month, with a separate regulation on multilateral interchange fees (MIFs) likely to be published simultaneously.

The new rules form part of the Commission's broader aim to promote a single European Payments Area (SEPA) and will seek to create a more competitive payments card market that reflects the explosion in the use of online and mobile payments.

MIFs are charges paid by a retailer to a cardholder's bank as part of an electronic payment card transaction, whether through a debit or a credit card. Nominally, it is designed to share the cost of processing payment card transactions between the buyer and seller.

Interchange fees set for cap under new rules

Retailers pay the fee but usually incorporate a hidden charge within their goods for the cost of the fee. They do not like the fee and would like to see it capped, limited or even banned. Many politicians have argued that if this happens, consumers would benefit from lower prices for goods as a result.

The draft proposal, seen by EurActiv, states that a new regulation – to be published with the PSD update – will cover "multilateral and bilateral interchange fees for all consumer debit and credit card transactions and electronic and mobile payments based on these."

That is likely to mean stricter limits placed on such interchange fees, although there are doubts as to whether corporate cards would be covered by the new rules.

Monnet scheme collapsed when participants bailed out

Whether the new rules will genuinely open the market to new players is a point of contention.

"The MIF model distorts competition in the payment market in a way which inhibits innovation and prevents new players from entering the market," said Ruth Milligan,

Continued on Page 2

Continued from Page 1

the senior advisor on payment systems with EuroCommerce, the European traders federation.

EuroCommerce believes such barriers must be removed to allow merchants and consumers to fully benefit from new technologies.

Consumer groups agree, although for different motives. "MIFs thwart innovative, cheaper and more secure payment means from emerging because most banks prefer cards for their MIF-related income," said Monique Goyens, the director-general of European consumer group BEUC.

"The fact that a few big players dominate the card market is convenient for banks, but bad for consumers," Goyens said.

However the only tangible attempt to create a pan-European card scheme that would compete with MasterCard and Visa (see background) failed two years ago. The so-called Monnet Project involved 24 banks from seven countries.

Questions over duopoly

The Monnet partners cited legal uncertainty, the overall economic situation in Europe and doubts about the sustainability of the business model as reasons for ending the project.

Meanwhile, incumbent operators claim that treating MasterCard and Visa as a duopoly no longer rings true, and rules designed to curb their business will allow other players to jump in.

Forcing down MIFs could exclude from the new regulation very large players such as American Express and Paypal, said MasterCard Europe President Javier Perez.

"If interchange fees needs to change, the Commission could effectively give preference to the Amex card model," Perez told EurActiv in a recent interview.

The current draft PSDII contains no direct reference to the Amex business model, which would not be affected by changes to interchange fees.

Debate surrounding the likely impact of the regulation on consumers is also likely to ignite disagreement, not least amongst consumer representatives themselves.

"Consumers are fed up having to perk up card company and bank balance sheets. Courts and regulators have time and again ruled interchange fees unfair and so plans by the European Commission to finally regulate them would be a very welcome move," according to BEUC's Goyens.

New rules for existing technology

However other consumer groups are not convinced that reductions in MIFs would be reflected in price reductions.

Last month Spanish consumer group ADICAE, one of Europe's 10 largest, called on the Commission to refrain from further reductions on MIFs if the measure is not accompanied by a regulation on the costs and interest consumers pay for using payment cards.

Spain is one of the few countries where strict curbs on MIFs have been introduced, and ADICAE claims that analysis of the Spanish experience suggests the reductions have caused "serious damage to consumers", and showed no benefits in terms of costs.

The new directive is also designed to deal with the fast pace of change within the payments market, however, including innovations in social behaviour and product development.

The boom in smartphone and tablet use may have spurred the Commission to revisit the directive now, but if innovations continue at the rate of the last five years, the current update may itself be outdated before long.

Cultural differences challenge European single payments area

New rules to promote a Single European Payments Area (SEPA) will be presented this month, but the EU executive faces cultural as well as regulatory hurdles in attempting to promote online and mobile payments across the EU.

The European Commission is set to publish its update to the Payment Services Directive (PSD II) aiming to level the playing field between incumbent card, internet, and mobile payments services providers, and new providers entering a rapidly changing market.

The EU executive wants such payments to reach a broader market and proposes measures to bridge standardisation and interoperability gaps across countries that still maintain strictly national markets in relation to rules for payments.

The draft proposal, seen by EurActiv, identifies lack of standardisation and interoperability between different payment systems – cards, the internet and mobile phones – and cross–border differences within the EU as a challenge to SEPA.

One of the key challenges facing the EU executive is not regulatory but cultural, with widely varying payments habits across member states reflecting different national traditions and behaviours.

Contrasting attitudes

In the United Kingdom, where payments cards are more frequently used than any other EU country, credit and debit card spending is set to almost double over the next decade, according to a report issued this month by the by the UK Cards Association, an industry trade body.

In 2012, nine out of 10 UK adults

Continued on Page 3

Continued from Page 2

carried a debit card, equating to almost 47 million debit card holders across the country. The number grew by around a million compared with 2011, a figure that is in line with growth seen over the past decade.

Innovations in technology which make card use more convenient will drive the upswing, the report said, helped by younger people who have grown up with cards and are already in a strong habit of using them.

This reflects a global "payments readiness" index compiled by MasterCard which shows a wide variety of people across Europe who regularly use mobile payments. The index earmarks the UK as a likely testing ground for future mobile payments in Europe.

"The United Kingdom much more closely resembles the United States, Canada, and Australia than it does Germany, France, and Italy," according to the index.

Italians prefer cash

By contrast mobile payments in Italy "remain in the nascent stages from both a market and a consumer-readiness perspective," the index shows.

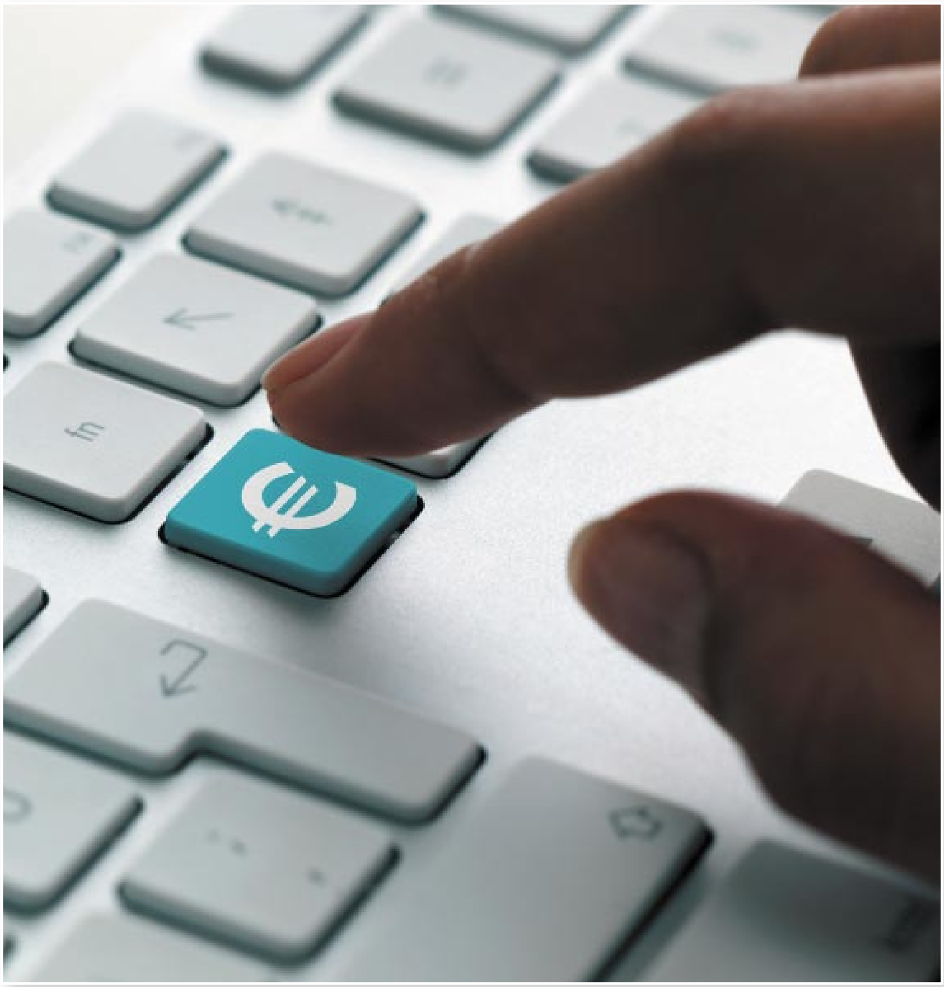
Although the index points out that financial and regulatory hurdles in the Italian market bear some responsibility, it also emphasises that Italian consumer attitude are more cash-friendly.

"Consumers will require significant education and marketing efforts to raise both their awareness of and willingness to use the technology" if they are to catch up, the index says.

The British-Italian comparison is reflected in broader differences between the EU's eastern and western states.

The use of modern payment methods – whether cards, mobile or internet – reflect the findings of the Europe B2C Ecommerce Report 2013, which showed the largest European countries like the United Kingdom, Germany and France dominating the market.

However, it also found that the fastest-growing markets are in Central Europe and the austerity-hit Mediterranean.



Here the future of a SEPA in which mobile and internet payments become a pan-European reality shows promise. Even if the these countries have shown less absorption of new payments systems, their internet accessibility is increasing far more rapidly than in West European states, which start from a higher level.

Moreover, the new SEPA landscape envisaged by the Commission's paper seeks to maintain flexible governance over new entrants into the retail market, new forms of payment, and to reflect new ways in which Europeans are buying online.

Level playing field

With Europe maintaining its position as a leader of online retail, there is no reason why the existing differences should not level out rapidly.

Ecommerce Europe, a trade group, says that 2013 will see a definitive break with the past as the relative share of e-commerce conducted over mobile phones and tablets – rather than conventional computers – reaches new highs.

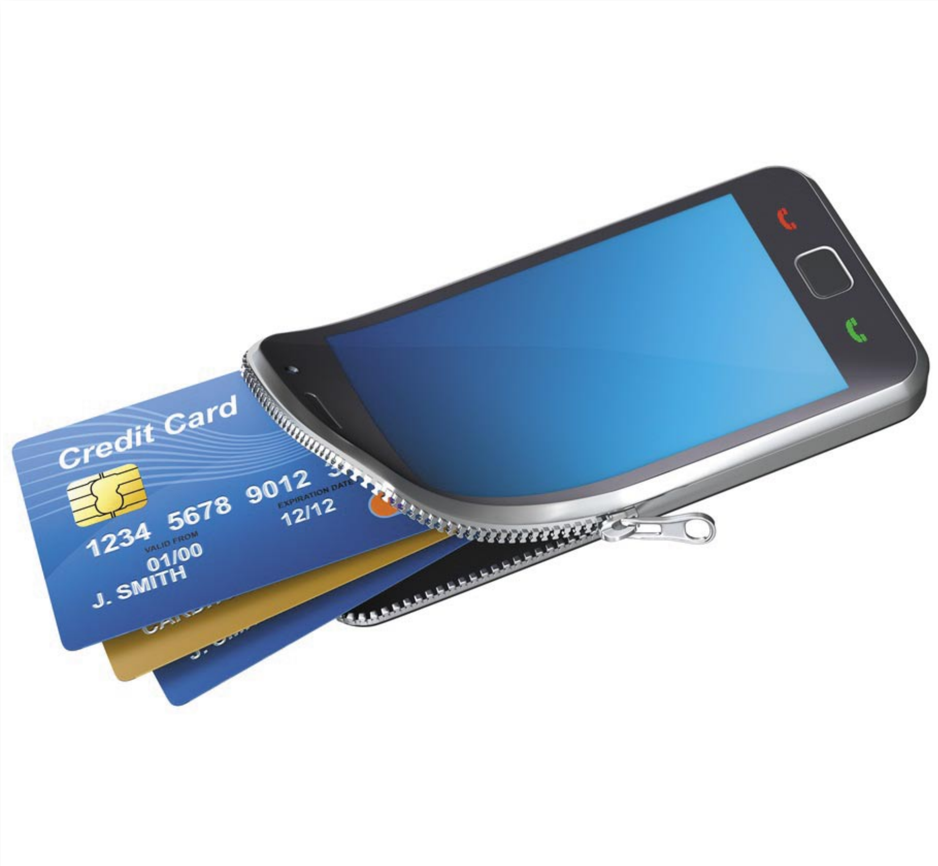
Wijnand Jongen, the executive committee chairman of Ecommerce Europe, said the buying behaviour of consumers in Europe's largest countries was "like youngsters" in e-commerce terms, whereas in the emerging countries, "we are like toddlers learning how things work and what the opportunities are".

"Over the next five-to-ten years, e-commerce will be immersed in every part of life, consumers will adapt, and this adaptation is exponential," Jongen said.

"Innovation and entrepreneurship in e-commerce is being promoted on a European level, also through the outstanding European companies leading the way into the new era of interactive retail," said Marc Lolivier, director-general of the French E-Commerce Association FEVAD and vice president of Ecommerce.

These buying opportunities, no less than technology, will play a key role in how the new SEPA landscape emerges.

New mobile payment systems pose regulatory, security challenges



An updated Payment Services Directive (PSD II), to be published by the European Commission this month, will struggle to cover regulatory and security challenges posed by a range of new mobile payments services expected to explode onto the European scene over the next two years.

The new rules form part of the Commission's broader aim to promote a single European Payments Area (SEPA) and will seek to create a more competitive payments card market that reflects the explosion in the use of online and mobile payments.

According to a draft of the new rules, the EU executive earmarked as a key source of concern "the legal vacuum for certain newly emerged internet service providers, such as third-party service providers offering online banking-based payment initiation".

This legal vacuum risks impeding innovation and appropriate market access conditions, according to the paper, and the EU executive therefore proposes bringing them within the ambit of the regulation and giving such new operators decision-making powers within a reformed governance structure for SEPA.

Mobile payments take many forms

"Digital wallets" can refer to a wide range of new applications offering simple payment methods to consumers as they gain popularity in Europe.

A key difference distinguishes wallets that act as a software platform to the consumers' existing banking cards and facilities, and those that offer a distinct payments service.

MasterPass and Google Wallet are examples of open systems that enable users to access their banking cards using software.

Google Wallet requires Near Field Communication (NFC) technology, only available on certain smartphones and tablets, but both services allow users to link to their existing cards through their mobile phone to make transactions in shops.

At the moment these services are much more popular in the United States.

Apple's Passbook, by contrast, enables users to manage movie, concert, airline tickets and loyalty cards, giving users information and time-based notifications on when tickets or coupons are nearing their due date. Unlike Google Wallet and MasterPass, however, users cannot use their debit or credit cards to make transactions.

Paypal offers users with an email address the chance to send and receive payments online, and has also entered the mobile payments market.

New directive covers third-party providers

Although the new PSDII regulation hopes to catch all these new types of payment methods within its regulatory scope, there are doubts about how far innovations might be able to elude the new rules.

"Market-based solutions are the best way to ensure a competitive payments landscape. However, if there is to be legislation it is crucial that all parties operating in the payments space, including third-party [such as Amex and PayPal] and domestic schemes, are included to ensure a true level playing field," said Jason Lane, who leads MasterCard's European market development.

But such regulation of digital wallets is only one side of a multifaceted regulatory challenge, with security issues also to the fore.

Dunhill has developed a 'Biometric Wallet' so secure the company claims it is "virtually indestructible". When closed it has a locking mechanism that can only be opened by the owner using a fingerprint scanner on

Continued on Page 5

Continued from Page 4

the back of the case. The Biometric Wallet can be linked to a mobile phone and if the phone is more than five metres away from the wallet an alarm sounds.

The danger to digital wallets lies not with pickpockets and thieves but long-distance hackers able to enter online accounts.

In the United States, where mobile payments are more widely used than Europe, mobile phones were targeted in more than 40% of all robberies in New York and 38% of all robberies in Washington last year.

"It's a simple formula for crime: no password plus instant access to online accounts equals fraud, identity theft and privacy loss," said Robert Siciliano, chief executive of the security website IDTheftSecurity.com.

The European Payments Council – the decision-making body of the European banking industry whose main task is the development of SEPA – on 2 July published a white paper on mobile wallet payments for stakeholder review over the summer.

The paper is intended to help lay the foundations of a secure ecosystem to enable all payers and payees to make and receive mobile payments across SEPA.

Today, mobile wallets are in the early stages of development. No one knows exactly how the mobile wallet marketplace will evolve in the coming years. Harmonisation and interoperability of systems and security issues will be key to how much trust Europeans place in them.

Economist: Lower card fees did not benefit Spanish consumers

The Spanish experience of lowering multilateral interchange fees for debit and credit cards was not positive, says Gustavo Matías Clavero, who is pessimistic about the European Commission's chances of achieving its goal of a single payments area through an updated Payments Services Directive.

Gustavo Matías Clavero is an economics professor at the Autonomous University of Madrid and serves as an expert at European Economic and Social Committee for its forthcoming opinion on the European banking union project. He spoke to EurActiv's Jeremy Fleming.

What did your research into the effects of decreases to multilateral interchange fees (MIFs) - charges incurred by retailers when consumers use credit and debit cards - in Spain?

The Spanish experience hasn't been positive and holds five or six negative consequences on the economy: income adjustments for the agents and imbalances of the market; fee and price upsurges for consumers; lower growth of electronic payments versus cash; more underground economy; less innovation; less convergence with the rest of Europe, and so on.

When Interchange Fees are forced down, issuing and acquiring banks, damaged by lower revenues, defend their income statements [by] increasing other costs. These new costs will be paid by consumers or even by the merchants: different kinds of cardholder fees and interest rates in credit and debit cards, or new ATM costs.

On the other hand, merchants do not take advantage of the savings of the new merchants service charges reductions applied by acquiring banks trying to lower consumer prices. Instead they use them to improve their margins and profitability, mainly because at the moment the retailers are badly hit by the austerity plans which remain in Spain and other European Union countries less open to competition, innovation, productivity and competitiveness.

Do you think there is a direct correlation between lower MIF and higher consumer charges. After all the Commission is confident this did not happen in France?

This was reported on many occasions by consumer organisations before we proved it through the study of several professors from Spanish universities including myself, developed using official statistics and data.

Our findings were also upheld by other studies in Spain, which demonstrate that cards use has slowed down in Spain and other countries since 2008, contributing to lower private consumption and hence a lower GDP and employment rate.

What the Commission says about France is very different from what the Fédération bancaire française and several French consumer organisations have stated. The problem is that the European Commission just addresses the merchants' opinion and forgets about all the other actors, and does not consider other costs and benefits of the means of payment that affect directly consumers and the economy as a whole.

What are the challenges facing implementation of the new Payment Services Directive?

Continued on Page 6

Continued from Page 5

Judging by the rumours after the white paper, which were submitted after minimum discussion despite its importance, the Commission wants to amend the last three directives related to payments methods and repeal the 2007/64 directive which is very important and has not even completed its transposition.

It is laudable the goal to try to achieve an efficient, transparent and competitive payments market similar to the most effective member state market. But that will never happen and will be pure rhetoric if we don´t combine idealism with the right realism.

The reality is that in the EU we have more than 28 payment systems. In the SEPA there are more than 33 (27 until now, 28 with Croatia starting from this month, including the countries involved in the payments methods unit: Iceland, Liechtenstein, Monaco, Norway and Switzerland). Making them converge is different from trying to converge to the best one. It is illusory to achieve it through many more regulations that only increase the complexity and furthermore – as in the case of Interchange fees – they threaten to have an impact opposite to that which they were seeking.

The proposal is to create a new SEPA board, with representation from many different stakeholders. What do you think of that idea?

All participation and transparency will always be welcomed, so long as it does not turn into the joke about the committee that invented the camel by designing a horse.

Until now, in many EU projects, such as the draft regulation that we are dealing with, representatives have helped little. The Single Euro Payments Area already has a European Payments Council formed by 74 members representing banks, national banking associations and institutions from the European Union payments system.

Ideally, the new council should be assisted by a powerful observatory body with the ability to request statistics. It should also be designed as a decision-making forum coordinated with all the actors involved in the unification of national payment systems at European level. But so far it has not worked for the many years since its existence. Until now it has failed to remove the barriers and limitations which would enable the eurozone to standardise an area and break down the borders to electronic monetary transactions.

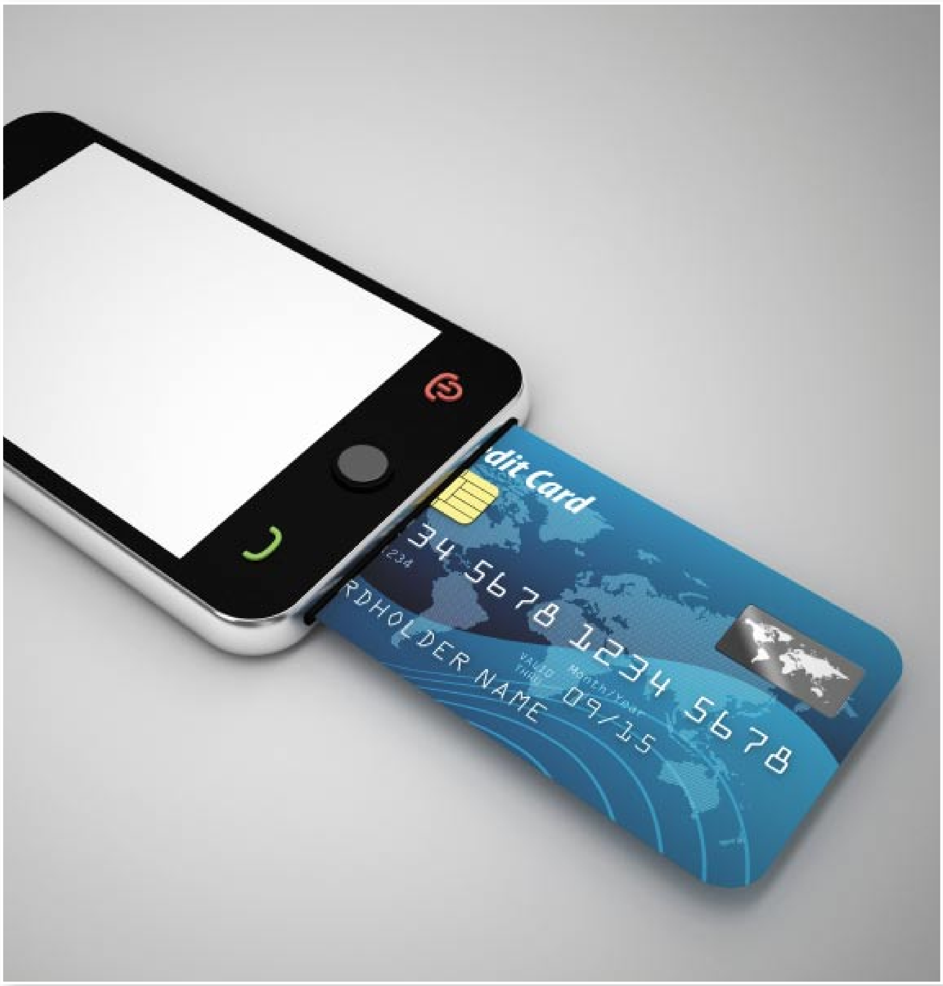
Can regulation keep up with innovation in this sector?

Regulations often just act as a hindrance to innovation, whether directly or in a roundabout way.

The past decade has shown us that the EU is losing the global battle to become the first and most innovative knowledge-based economy. Its legislative archives contain more than half a million rules. But entrepreneurs or innovative spirits are sometimes held back by regulation, whilst, according to Schumpeter technical and financial innovations, should be fostered by a competitive environment [that is] conducive to risk and benefit.

Thus, the problem is normally greater for innovators when new rules suppress the competitive environment, which the regulators would like to believe they are improving.

Academic says EU payments regulation will dampen innovation



An updated Payment Services Directive (PSD II) that aims to embrace new mobile payments methods could end up acting as a hindrance to entrepreneurs, a leading Spanish academic told EurActiv.

The Commission is set to publish its update to the Payment Services Directive (PSD II) this month, with a separate regulation on multilateral interchange fees (MIFs) likely to be published simultaneously.

The new rules form part of the Commission's broader aim to promote a single European Payments Area (SEPA) and will seek to create a more competitive payments card market.

MIFs are charges paid by a retailer's bank for processing a payment and aim at sharing transaction costs between the buyer and seller.

But Gustavo Matías Clavero, an economics professor at the Autonomous University of Madrid, doubts that the 28 EU states could successfully converge into one payments area.

"It is illusory to achieve it [SEPA] through many more regulations that only increase the complexity and furthermore – as in the case of MIFs – threaten to have an impact opposite to that which they were seeking," Matías Clavero said in an interview.

Matías Clavero emphasised that his research into Spanish efforts to lower MIFs had demonstrated no consumer benefits. The issue is hotly contested between consumer groups.

Matías Clavero said that when Interchange fees are forced down, "issuing and acquiring banks, damaged by lower revenues, defend their income [by] increasing other costs." Consumers or merchants will pay the price through cardholder fees, higher interest rates on credit and debit cards, or new ATM costs, he said.

He was also challenged the EU executive's contention that there have been no negative impacts on consumers in France, where MIFs were also lowered.

"What the Commission says about France is very different from what the Fédération bancaire française and several French consumer organisations stated," Matías Clavero said, adding: "The problem is that the European Commission just addresses the merchant's opinion and forgets about all the other actors, and does not consider other costs and benefits of the means of payment that affect directly consumers and the economy as a whole."

In general, Matías Clavero seemed pessimistic about the chances that PSDII would foster innovation.

He was unimpressed by proposals in the latest draft for a new SEPA governance system to be put in place, consisting of a new board with a wide range of stakeholders.

"All participation and transparency will always be welcomed, so long as it does not turn into the joke about the committee that invented the camel by designing a horse," he said.

The European Payments Council, which already exists as a stakeholder representative group to help establish SEPA, "has failed to remove the barriers and limitations which would enable the eurozone to standardise an area and break down the borders to electronic monetary transactions," he said.

Asked whether the new PSDII would be capable of keeping track with innovation in the sector, he suggested it was more likely to hinder it. "The problem is normally greater for innovators when new rules suppress the competitive environment which the regulators would like to believe they are improving."

Consumer groups divided over benefits of lower payment-card fees

Forthcoming European Commission proposals aimed at reducing charges for payment cards have ignited a debate over whether consumers will benefit, based on previous experiences in Spain and France.

The Commission is set to publish its update to the Payment Services Directive (PSD II) this month, with a separate regulation on multilateral interchange fees (MIFs) to be published simultaneously.

The draft proposal, seen by EurActiv, states that the new regulation will encourage "downward convergence of costs and prices for payments services users", which is almost certain to mean stricter limits placed on interchange fees.

MIFs are charges paid by a retailer's bank for processing a payment card transaction. Retailers usually incorporate the fee as a hidden cost within the good they sell, leading some consumer and retailer organisations to call for their elimination.

But whether consumers will benefit in the end remains bitterly contested.

"Whether the price of the goods will decrease when MIFs are lowered depends on retailers," said Monique Goyens, director-general of European consumer group BEUC.

Spanish research

"Considering the competitive market situation they [retailers] face, a downward pressure on prices is the expected outcome," Goyens added.

In considering reductions to MIF, "nobody has seriously taken into consideration the consumers' interests, who risk being the final loser here," said Pascual Fernández Martínez, professor of economics at Universidad Rey Juan Carlos in Madrid.

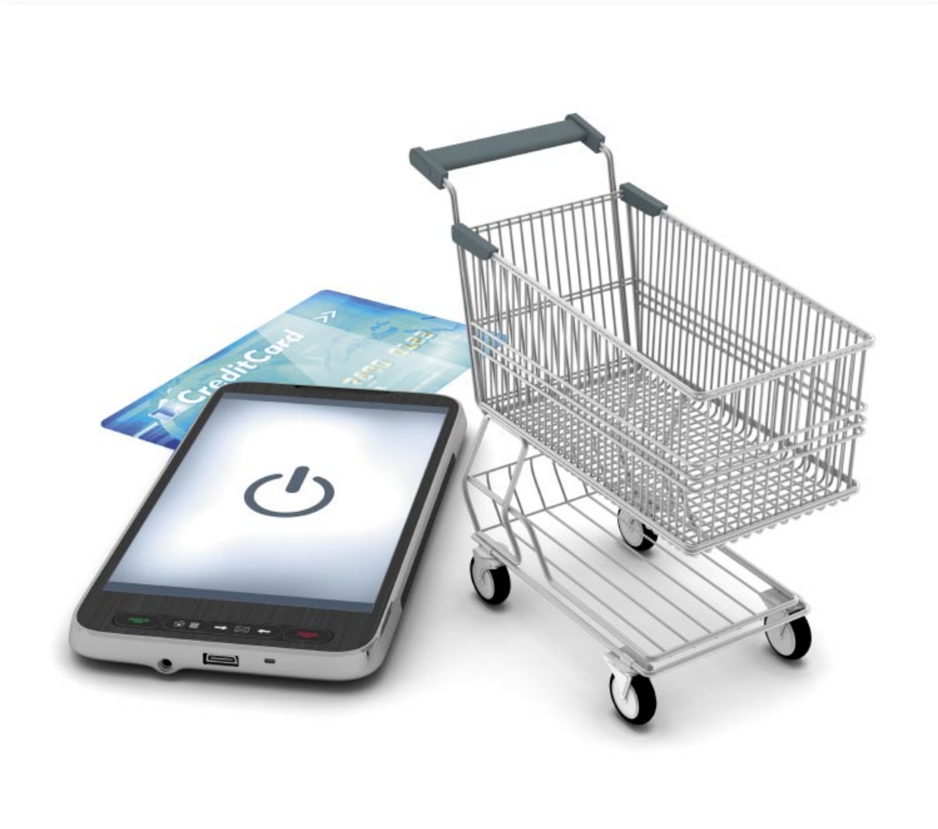
Martínez has researched the position in Spain where interchange fees were reduced by more than 57% between 2006 to 2010.

"I must come to the conclusion that consumers did not benefit at all from this reduction. Retailers have. Undoubtedly. This reduction saved them almost €2.75 billion over the five-year period," he said.

Martínez said lowering the MIF led banks to lose fees, which they sought to regain by increasing their charges to consumers. "The consumer ended up paying for the retailers' savings," he said.

Ruth Milligan, the senior advisor on payment systems with EuroCommerce, the European traders federation, contends these claims do not weigh up. She said that an increase in sales resulting from the lower price means that banks do not experience losses.

"The price of the transactions may go down, but with more overall transactions, they [banks] do not experience a difference," Milligan said.



Consumer group not convinced of benefits

That does not convince Spanish consumer group ADICAE, one of Europe's 10 largest, which last month called on the Commission to refrain from further reductions on MIFs, citing the Spanish experience.

But Goyens points to the example of France, where interchange fees were also lowered. "Here [in France] a reduction of the interchange fees did not result in increased card holder fees," she said.

The variety of consumer-group opinions on the issue adds to the sense of confusion over what the real impact of MIF reduction will be, however.

The Italian consumer group Movimento Difesa del Cittadino stands

Continued on Page 9

Continued from Page 8

in opposition to BEUC's point of view. "The reduction in interchange [in Spain] has clearly harmed consumers by raising cardholder fees and reducing card benefits," said Antonio Longo, the group's chairman.

Back to cash

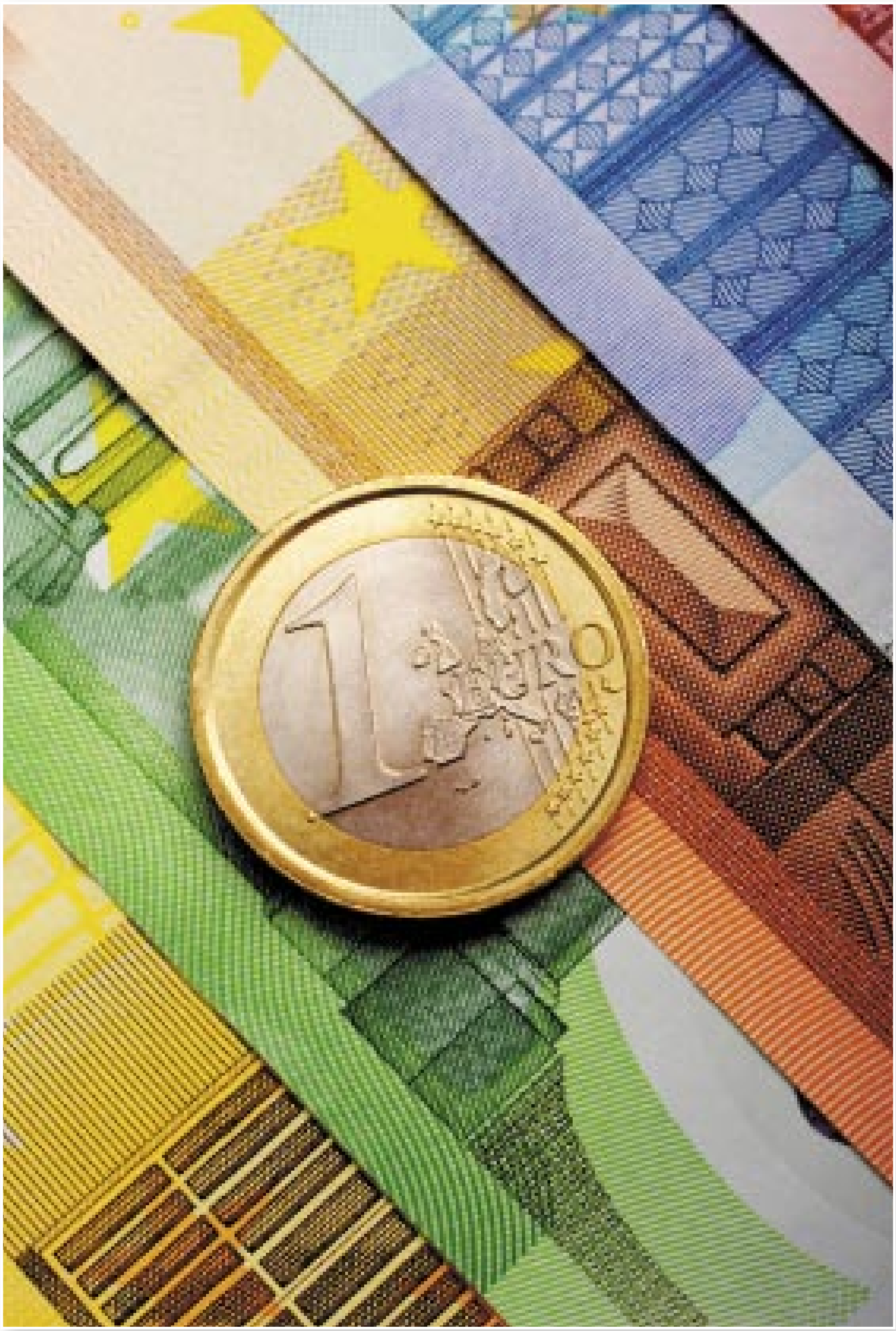
Meanwhile, MasterCard claim that lower interchange fees would lead to consumer cost rises, which they believe would drive consumers to use more cash.

"Ultimately, it would be bad for the European economy at a time when spending needs to be encouraged to stimulate recovery and where governments are trying to reduce the black economy in order to increase their revenues for budget purposes," said MasterCard Europe spokesman Jason lane.

If there is confusion over the impact of the forthcoming new rules on consumers, then the updated PSDII should at least introduce measures to ensure greater consumer involvement in monitoring the effects of the new rules.

"The protection of consumer interests" is listed as a specific objective of PSDII in the preamble, and changes to the governance of the Single European Payments Area – including the establishment of a new steering committee with consumer representatives – seeks to "empower all stakeholders to take a more active role in the conception and realisation of payments governance".

That should theoretically give consumer groups more of a voice in the policymaking process.



For information on EurActiv Special Reports...

Contact us

Delia Nicolaescu
events@euractiv.com
tel. +32(0)2 788 36 72

Ross Melzer
publicaffairs@euractiv.com
tel. +32(0)2 226 58 17

Other relevant contacts:

Rick Zedník
ceo@euractiv.com
tel. +32(0)2 226 58 12

Frédéric Simon
executiveeditor@euractiv.com
tel. +32(0)2 788 36 78