AMERICAN EXPRESS

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Submission in response to Issues Paper – Regulating to reduce Merchant Service Fees

Thank you for inviting industry consultation on the matters raised in this Issues Paper. American Express New Zealand welcomes the opportunity to comment.

Set out below is our response to some of the issues raised.

American Express supports the idea of supporting the retail sector, particularly in the current environment created by Covid-19.

However, before further steps are considered, we submit that a thorough and independent analysis of payment costs for consumers and merchants in New Zealand should be undertaken.

The Issues Paper operates on the assumption that the costs of payments in New Zealand is high compared to regulated markets. Our data does not support this. Regulation should only be used where there is clear market failure. We think it is important that reliable and independent data supports any regulatory decisions.

The American Express Model

American Express is a global financial services company who is an issuer of cards, a merchant acquirer of its transactions and a network operator in 136 countries. We have been operating in New Zealand for more than 40 years.

American Express has a substantially different business model to other providers. Our closed-loop network means that most American Express-branded cards worldwide, and the transactions on these cards, are issued and acquired by American Express itself. This contrasts with the Visa and Mastercard networks who don't issue or acquire transactions, with these processes undertaken by their member financial institutions.

Despite being a global brand, American Express is a niche player in New Zealand with a small share. We estimate we have approximately 5.5% share of the value of credit and charge card transactions in New Zealand and we do not issue debit cards in New Zealand. As a small player, American Express brings competition, innovation and increased consumer choice.

Given our lack of market power, American Express is not a 'must take' card. No consumer or merchant must hold or accept an American Express product. This is not true for Visa and Mastercard where virtually every merchant who accepts cards will accept, and every consumer who holds a credit card will hold, a Visa or Mastercard.

Merchants and consumers choose American Express products because they recognise the value American Express delivers. For example, increased business from our high-spending cardholder base who have an average transaction size of approximately 1.5 times the rest of the card industry. Our products are also an important cash flow tool for many small businesses. American Express is able to deliver this value as a result of its investments and efforts targeted marketing, business-building initiatives, rewards and other cardholder and merchant benefits and services.

American Express has always had a different fee structure to other providers. Our fees to merchants are simple, transparent and do not vary depending on the type of American Express Card or how the merchant accepts the card. The merchant fee is the same whether contactless or not.

American Express has no multilateral interchange fees or scheme fees that set a floor for merchant fees. American Express generally negotiates its fees bilaterally with each merchant. Even in cases where merchants contract with a third party for American Express merchant acceptance, our principles remain the same.

We also continue to invest in initiatives to drive more commerce to businesses including small merchants through programs such as Shop Small which American Express founded and launched in New Zealand in 2020 to support small businesses during Covid-19. Shop Small drove approximately $5 million in spend to small businesses and supported over 15,000 small businesses across New Zealand. We offered all our American Express Card Members a $50 incentive to support their local and small businesses at the end of 2020 and invested in a nationwide movement to promote shopping small.

Data Integrity – payment costs in New Zealand

We note MBIE's 2016 study through its Retail Payments System in New Zealand issues paper. American Express' view of that paper was that the data used led to the wrong conclusion that New Zealand merchants pay more for electronic transactions compared to regulated markets. We think this same error has been repeated in the Issues Paper, by relying on Retail NZ survey data, resulting in the incorrect conclusion that merchant service fees in New Zealand are high based on international comparisons.

We asked independent Australia and New Zealand payment consultant Michael Ebstein from MWE Consulting (**MWE**) to test this hypothesis by comparing New Zealand payments data to Australia, as its nearest comparable regulated jurisdiction. We also asked MWE to test the figure from Retail New Zealand used by the Government in its pre-election announcement to regulate merchant service fees – that small businesses in New Zealand pay $13,000 a year more in merchant fees than similar Australian businesses. MWE's full analysis is **attached.** It finds that:

- There is only a relatively small difference in the average cost of accepting a card transaction in New Zealand compared to Australia. In 2019, the average cost of acceptance in New Zealand was 0.72% compared to 0.69% in Australia.
- The total average cost of acceptance in both countries reduced in 2020.
- Transactions processed via EFTPOS in New Zealand do not incur merchant fees unlike in Australia where the average fee has been stable for a few years around 0.27%. This is a key factor in assessing the costs of payments in New Zealand to comparable jurisdictions.
- Based on 2019 data on the average overall costs of payments in New Zealand compared to Australia, to arrive at a figure that small businesses are paying $13,000 more per year in New Zealand would require an average merchant turnover of $43.33 million. Retail NZ data indicates that on average, retail annual turnover is $3.487 million.

With the overall costs of payments in New Zealand comparable to Australia (where the costs, as recognised by the Reserve Bank of Australia are low by international standards), we submit there is no market failure and case for regulation.

MWE also notes that forming a view of payment costs in New Zealand is challenging as the data from the RBNZ and Statistics New Zealand does not provide the granularity of the Australian data published by the Reserve Bank of Australia. Further there are also classification issues in the New Zealand data where contactless debit is sometimes classified as 'credit'.

It is important that before any regulatory decisions are made, MBIE has access to reliable and independent data to ensure that there is a robust evidential basis for any necessary regulatory intervention. We submit that the next step in this process should be for MBIE to conduct a thorough and independent analysis of payment costs for consumers and merchants in New Zealand.

Regulation needs to consider different business models and share

If regulation is pursued, it should be targeted and proportionate to the perceived market failure and aim to minimise the impacts on those with no market power. It is particularly critical when considering price regulation that distinctions between schemes that operate with market power or on the basis of multilateral agreements and those that do not, such as American Express, are taken into account.

Any regulation considered should appropriately account for different business models across the industry, with clear exemptions where regulation does not make sense in the context of a specific business model. American Express welcomes the MBIE's recognition that three-party schemes do not have interchange fees and the fact that its initial proposal for interchange fee regulation is accordingly applicable only to open party debit schemes. Should the initial proposal be adopted, we urge the MBIE to ensure that this position is reflected in a clear exemption that provides legal certainty for three party schemes.

Taking a one size fits all approach can have unintended consequences and reduce market competition, to the detriment of merchants and consumers. As noted above, American Express has a substantially different business model to other providers with no interchange fees and a small share. The reality is that American Express acceptance is a choice and American Express does not force its pricing or any other commercial terms on merchants. Merchants who choose to accept our cards to do because they recognise the value we deliver. However, in jurisdictions with payments regulation, it generally has a disproportionate impact on smaller players like American Express.

For example, even though American Express does not have interchange fees, interchange regulation in Australia has led to a greater impact on American Express' merchant service fees than to those for Visa and MasterCard. Regulation intended to address concerns arising from the practices of the dominant players often has a more significant impact on smaller competitors.

Any regulation should be targeted to ensure that those without market power can compete with the dominant players ensuring choice and product innovation.

The need to balance consumer and merchant needs

American Express makes the following points about any potential regulation:

- Any regulation should be based on independent data sources of the true costs of payments in New Zealand. The experience in Australia has demonstrated that regulating in this area is extremely complex with the Reserve Bank of Australia having to change its regulation periodically as industry adapts to the regulation. Accordingly, it helps if there is an agreed and independent source of data at the outset.
- Lowering interchange resulted in increased costs and reduced benefits for consumers in Australia – through surcharging or through changes to consumer product which increase their cost or reduce their value. There is no conclusive

evidence to suggest that regulation has driven lower retail prices for consumers. Rather, we believe the result has been higher retail profits, particularly for large merchants.

- Any regulation should account for the fact that merchants derive significant value from payments. Components of the value to merchants include the payment guarantee, prompt and efficient payment, processing services, marketing and rewards programmes and the wider social benefits associated with electronic payments.
- We also note that substantial investments are necessary on the part of payment providers to build and maintain a competitive payments network with extensive services and scale (fraud prevention, chargeback protection, technical standards and operations to ensure global operability for example). Investment pressures have only increased with the evolving nature of the payments landscape. Any regulatory intervention needs to be mindful of this to ensure providers can continue to innovate and offer extensive services to both consumers and merchants.

Surcharging

If regulations are implemented to reduce the cost of card acceptance to merchants, then it makes no sense to also give merchants the ability to surcharge. In effect – why go to all the effort to regulate cheaper card acceptance prices for merchants – but then give merchants the ability not to pay for them anyway.

Surcharging is harmful to consumers, brand-damaging to schemes, prone to exploitation by merchants and disproportionally impacts providers who lack market power.

As discussed above merchants derive significant benefits from card payments. In the two-sided market between cardholders and merchants it does not make sense that merchants should be able to 'free-ride' by pushing 100% of the legitimate cost of their card payments costs to consumers.

Surcharging is prohibited in many comparable international jurisdictions. The rationale for this is that it's a bad consumer experience, it discriminates against alternative providers at point of sale and if costs are low, there is simply no need to allow surcharging.

Surcharging is also inconsistent with the position of competition and consumer regulators who have spent many years pursuing 'single pricing' for consumers (whether it be GST, airline baggage fees or administration charges). We don't believe there is anything that should distinguish payments from the consumer benefits of single pricing.

Surcharging also has a disproportionate impact on those without market power. As can be seen form the Australian experience, industries without monopoly or significant market share often had excessive surcharging and industries with more competition did not surcharge. Similarly, for card products – those without market power that are not 'must take' like American Express were often disproportionately surcharged.

Comments on supplementary options

Should interchange fee regulation be pursued, we submit this is best complemented by increased fee transparency measures. 'Other price regulation', for example, merchant service fee regulation, has not been done in any comparable jurisdiction in the world, is an extremely blunt instrument and a drastic step that could serve to reduce competition, consumer choice and prevent investment in New Zealand.

We would welcome the opportunity to discuss this submission with you, including to provide further detail on the MWE analysis attached – my contact details are enclosed.

Ngā mihi

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New Zealand Country Manager
American Express

Encl: MWE review of merchant service fees

MWE Review of the MBIE Dec 2020 Paper on Merchant Service Fees

MBIE is seeking feedback on its commitment to regulate merchant service fees to reduce costs to retailers. This appears to be largely based upon an estimate that an average merchant in New Zealand pays $13,000 more annually in merchant service fees than an equivalent merchant in Australia. At the outset, we sought to measure the average merchant service fee in each country.

Estimate of average merchant fees in Australia

The RBA publishes detailed data on the payments market in Australia and MWE utilises this data to publish a monthly analysis of the payments arena with the MWE Cards Report used by many financial institutions in their planning and management of their payment businesses. The following estimate of the average merchant fees in Australia is based on the data from those sources. The sole metrics not based upon published empirical data are the split of the debit market into scheme and eftpos and the share of the credit and charge market attributed to Diners Club. These have been estimated by MWE.

We note that we have used the average merchant fees published quarterly by the RBA. In addition, we note the RBA reported that in 2018/19, the range of scheme credit between the smallest and largest merchants was from about 1.45% to about 0.70%; scheme debit ranged between about 1.1% and 0.45%; and eftpos between about 0.6% and 0.1%

Australia

	Card Scheme	Average 2019 fee	Market Share	Average Fee
Credit & Charge	Visa & MasterCard	0.90%	83.8%	
	American Express	1.39%	15.8%	
	Diners Club	1.78%	0.4%	
			100.0%	0.98%
Debit	Visa & MasterCard	0.51%	60.0%	
	eftpos	0.27%	40.0%	
			100%	0.41%
Total Market	Credit & Charge	0.98%	48.4%	
	Debit	0.41%	51.6%	
			100.0%	
Total Average Fee				0.69%

	Card Scheme	Average 2020 fee*	Market Share	Average Fee
Credit & Charge	Visa & MasterCard	0.87%	84.4%	
	American Express	1.33%	15.3%	
	Diners Club	1.90%	0.3%	
			100.0%	0.94%
Debit	Visa & MasterCard	0.45%	60.0%	
	eftpos	0.26%	40.0%	
			100%	0.37%
Total Market	Credit & Charge	0.94%	43.4%	
	Debit	0.37%	56.6%	
			100.0%	
Total Average Fee				0.62%

*The 2020 estimate is for the period Jan to Sep 2020

The MWE estimate of the overall average merchant service fee of 0.69% in 2019 is validated in the RBA's March 2020 paper "The Cost of Card Payments for Merchants." Graph 2 in this report shows the average merchant service fee for all cards in Australia has reduced from about 1.2% in 2002 to about 0.7% in 2019. The subsequent decline in the average fee in 2020 is a result of a marked increase in the share of transactions on debit together with reductions in the average fees for scheme cards.

Estimate of share of value of credit and debit in New Zealand

An estimate of the New Zealand market is more problematic as the data from the RBNZ and Statistics New Zealand does not provide the granularity of the Australia data and the metrics from Statistics New Zealand have been overstating the share of card transactions on credit by incorrectly classifying contactless debit as credit. When MBIE reviewed card payments in 2016, the difference was not great. Statistics NZ data showed the share of value as 46.9% on credit and charge and 53.1% on debit. This compared to data from the MBIE paper showing 42% on credit and 58% on debit. However, as contactless debit has grown, the most recent (November 2020) data from Statistics NZ shows credit at 60.2% and debit at 39.8%. In our MWE NZ Card Reports, we have been adjusting the Statistics NZ metrics by combining it with the C13 Card Spend in NZ series from the RBNZ. More recently, we have been able to access data prepared by Payments NZ. The share of value shapes up as follows with the Australian data included for comparison.

Share of Value (1)

Year	Statistics NZ		MWE amended *		Payments NZ**		RBA	
	New Zealand						Australia	
	Credit	Debit	Credit	Debit	Credit	Debit	Credit	Debit
2010	42.6%	57.4%	51.6%	48.4%			62.8%	37.2%
2016	46.9%	53.1%	51.3%	48.7%			54.9%	45.1%
2019	55.8%	44.2%	51.6%	48.4%	32.7%	67.3%	49.7%	50.3%
2020	60.2%	39.8%	48.1%	50.9%	31.0%	69.0%	44.8%	55.2%

*****MWE amended the Statistics New Zealand numbers by embedding the RBNZ card present and card not present values for credit card use in New Zealand with the total value of purchases as measured by Statistics New Zealand.

**Excludes card not present transactions

Share of Value (2)

Year	Statistics NZ		MWE amended *		Payments NZ**		RBA	
	New Zealand						Australia	
	Credit	Debit	Credit	Debit	Credit	Debit	Credit	Debit
2010	42.6%	57.4%	51.6%	48.4%			62.8%	37.2%
2016	46.9%	53.1%	51.3%	48.7%			54.9%	45.1%
2019	55.8%	44.2%	51.6%	48.4%	42.0%	58.0%	49.7%	50.3%
2020	60.2%	39.8%	48.1%	50.9%	41.0%	59.0%	44.8%	55.2%

*****MWE amended the Statistics New Zealand numbers by embedding the RBNZ card present and card not present values for credit card use in New Zealand with the total value of purchases as measured by Statistics New Zealand.

**Includes an estimate for card not present transactions

The MWE amended share above and in the MWE New Zealand Card reports has been prepared over the last year in an attempt to obtain a more accurate view of the payment card mix. The more recently available numbers from Payments NZ are considered to be more accurate, albeit that they do not include card not present. Below are our estimates of fees for 1) card present and 2) total transactions in 2019 and 2020.

Estimate of average merchant fees in New Zealand

New Zealand 2019 Payments NZ Share Data - Card present

	Card Scheme	Average 2019 fee	Market Share	Average Fee
Credit & Charge	Total	1.5%	33%	1.5%
Debit	Contactless	0.9%	11%	
	eftpos	Nil	56%	
				0.15%
Total Market	Credit & Charge	1.5%	33%	
	Debit	0.15%	67%	
			100%	
Total Average Fee				0.60%

New Zealand 2019 Payments NZ Share Data – Total Market

	Card Scheme	Average 2020 fee	Market Share	Average Fee
Credit & Charge	Total	1.5%	42%	1.5%
Debit	Contactless	0.9%	10%	
	eftpos	Nil	48%	0.15%
Total Market	Credit & Charge	1.5%	42%	
	Debit	0.15%	58%	
			100%	
Total Average Fee				0.72%

New Zealand 2020 Payments NZ Share Data - Card present

	Card Scheme	Average 2019 fee	Market Share	Average Fee
Credit & Charge	Total	1.5%	31%	1.5%
Debit	Contactless	0.5%	20%	
	eftpos	Nil	49%	
				0.14%
Total Market	Credit & Charge	1.5%	31%	
	Debit	0.14%	69%	
			100%	
Total Average Fee				0.56%

New Zealand 2020 Payments NZ Share Data – Total Market

	Card Scheme	Average 2020 fee	Market Share	Average Fee
Credit & Charge	Total	1.5%	41%	1.5%

Debit	Contactless	0.5%	17%	
	eftpos	Nil	42%	0.14%
Total Market	Credit & Charge	1.5%	41%	
	Debit	0.14%	59%	
			100%	
Total Average Fee				0.70%

Conclusions

- There is now only a relatively small difference in the average cost of scheme debit in New Zealand and in Australia.
- Transactions processed via eftpos in New Zealand do not incur merchant fees unlike in Australia where the average fee has been stable for a few years at around 0.27%.
- The average cost of accepting credit in New Zealand is higher than in Australia. The view of MWE is that any regulatory intervention in the cost of payments in New Zealand should be made within the context of the total payments environment and should, for example, consider that all payment options, including cash, have a cost.
- We assess the average fee in 2019 in Australia at 0.69% compared to 0.60% for card present in New Zealand and 0.72% for the total market in New Zealand.
- The average cost of total debit has been steady in New Zealand in 2019 and 2020 as the increase in volume in contactless debit has essentially been negated by a decrease in the fee per transaction.

In summary, our analysis indicates that the difference in average cost of accepting a card transaction in New Zealand is close enough to the established cost in Australia to indicate that any regulatory intervention would be unnecessary and unwarranted. This is particularly so until an accurate mix of card payments in the total New Zealand market is established. As far as the card present market is concerned, we cannot establish any sound basis on which to conclude that merchants in New Zealand are paying materially more than merchants in Australia.

The first point in the Executive Summary of the MBIE Review of Merchant Service Fees in New Zealand: Release of Issues Paper states, "In comparison to Australia, New Zealand businesses were paying on average $13,000 more per year in merchant service fees". The MWE analysis indicates that the average overall card fee in 2019 was 0.69% in Australia and 0.72% in New Zealand.

On an annual card turnover of $100,000, that would result in an additional fee to a New Zealand merchant relative to an Australian merchant of $30 and on a turnover of $1,000,000, an additional cost of $300. A difference of 3 basis points in the overall average fee requires an annual card turnover of $43.33 million to deliver an increase in merchant fees of $13,000. An indicative fee differential of 8 basis points in 2020 requires an annual card turnover of $16,250,000 to produce that same incremental cost.

Retail NZ data indicates that the average retail annual turnover is $3,487,000. Given this includes all payment types, it reinforces our conclusion that New Zealand merchants are not being material disadvantaged by overall card fees.

Michael Ebstein
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