18 February 2021

Competition & Consumer Policy Team
Building, Resources and Markets
Ministry of Business, Innovation & Employment
PO Box 1473
Wellington 6140
New Zealand

Submitted by electronic mail: competition.policy@mbie.govt.nz

Dear Competition & Consumer Policy Team,

Visa welcomes the opportunity to provide a submission in response to the Ministry of Business, Innovation and Employment's (MBIE) Issues Paper on *Regulating to Reduce Merchant Service Fees*. We appreciate the holistic approach reflected in the Issues Paper, given the importance of considering any intervention in the payments system with care.

As a company that values our longstanding relationship with the New Zealand Government, Visa is committed to working with MBIE as it considers the best way forward in ensuring that the digital payments system delivers benefits to consumers, businesses and the economy more broadly. We make this statement against the backdrop of sharing the Government's vision to sustain the nation's economic bounce-back.

For Visa, this includes supporting small businesses to thrive in domestic and global markets. This is especially important in New Zealand, where small businesses comprise the majority of New Zealand businesses[1],and have been significantly impacted by the shift in consumer behaviour in response to the COVID-19 pandemic. For payments, this has included an increase in consumer demand for online, mobile and contactless. In providing support, Visa is focusing on key areas, such as enabling small businesses to build an online presence, expand their customer base as well as empowering them to benefit from the innovation and security of digital payments[2].

[1] Ministry of Business, Innovation and Employment website. Defined as businesses with fewer than 20 employees, there are approximately 530,000 small businesses in New Zealand representing 97 per cent of all firms.
https://www.mbie.govt.nz/business-and-employment/business/support-for-business/small-business/

[2] Visa Economic Empowerment Institute (2021), "Small Business in the digital age: recommendations for recovery and resilience". ***https://usa.visa.com/sites/visa-economic-empowerment-institute/digital-financial-inclusion/small-business-in-the-digital-age.html***

This commitment has heightened relevance as we work together to ensure that New Zealand's digital payments system can support, and catalyse the Government's plan to keep the recovery moving forward. In this regard, payment networks, such as Visa, help to:

- Boost economic growth, create jobs, and increase tax revenue.
- Drive innovation and the digital economy.
- Increase financial inclusion, including through supporting small businesses.
- Create transparency in transactions.
- Deliver enhanced security for consumers, businesses, and financial institutions[3].

Visa notes with concern that MBIE is considering interchange fee regulation in an effort to reduce merchant service fees, because we believe this approach may do more harm than good for New Zealand consumers and merchants, especially small businesses. The frequently cited assumption that fee regulation helps to drive down payment costs ignores the fact that price ceilings inevitably reduce the total pool of available resources for investment and innovation in the payments system. With digital technology evolving faster than ever before, the consumer landscape is changing rapidly. Considering all of these current trends, introducing price controls for payments now would create unnecessary risks just as the New Zealand economy is on the cusp of launching into long-term recovery.

Price controls for payments would create distortions in the marketplace that would artificially limit and arbitrarily allocate the value delivered to consumers and businesses alike. If formal regulation of the payments system were to favour one set of stakeholders over another, that would upset the critical economic balance necessary to create shared value for all participants. Given this, Visa believes the best path forward for payments policy in New Zealand today is to build upon the strong tradition of industry-led, self-regulation conducted in close consultation with government. In this spirit, we would welcome a robust discussion about how best to ensure that all consumers and businesses can make informed choices from a wide range of payment products in order to select the features and value that best suit their individual needs. And perhaps most importantly, we are committed to working with all stakeholders to ensure that the payments system remains strong, stable, and secure as commerce becomes increasingly more digital.

As MBIE considers this and other potential interventions, Visa believes that it is also critical for MBIE to take into account the enormous success New Zealand has had in growing digital payments over many years. According to RFi Consulting[4], New Zealand has one of the highest penetrations of digital payments in the world, which has undoubtedly been a key factor that has enabled the country to manage the COVID-19 crisis far more effectively than many other parts of the world. Additionally, it is worth noting that innovation on the acquiring side -

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[3] For further details on the benefits of electronic payments to economies, see the Visa-commissioned report (2017), **Cashless Cities: Realising the benefits of digital payments***, https://usa.visa.com/dam/VCOM/global/visa-everywhere/documents/visa-cashless-cities-report.pdf* and Moody's Analytics (2016), **The Impact of Electronic Payments on Economic Growth**, ***https://usa.visa.com/dam/VCOM/download/visa-everywhere/global-impact/impact-of-electronic-payments-on-economic-growth.pdf***

[4] RFi Consulting (2014), **The Evolution of Cash: An Investigative Study – Summary of Findings July 2014**. Report commissioned by the Australian Payments Clearing Association.

and not regulation – results in long-term, sustainable cost reductions for small businesses.

Below, we share our insights on the fundamental role that market-based interchange plays in the payments system, Visa's global experience regarding the impacts of regulation, and principles to consider as MBIE assesses this topic. We expand upon these directly below, and in the "Submission on discussion document" that follows.

1. There is a value and cost to payments and not all transactions are the same

Visa makes significant investments to enable international and domestic face-to-face commerce and e-commerce, including by guaranteeing consumers' zero liability for fraudulent transactions and engaging in real-time fraud monitoring. We also enable our payments system participants to offer value-add services, including reliability, more efficient processing, advanced authorisation, and chargeback protections. In addition, operational resilience is essential for a thriving digital payments system, and Visa invests in resilience and security accordingly. Combined, these investments benefit New Zealand consumers and businesses – and have done so particularly during COVID-19 - by enabling and securing commerce and encouraging international spend into the domestic market.

Each payment transaction can carry a different set of charges and costs, depending on various factors, including card type, transaction type, value of the transaction and the type of merchant. These factors introduce varying degrees and types of risk, which require specific investment and effort for the payments network, and its payments system members to manage effectively. Transactions can include credit, debit, card-present, card-not-present, domestic, international, token, non-token, consumer, and commercial.

To provide an example of how transactions differ, Visa processes both **domestic and international transactions**, which have different costs, fees and value to the stakeholders associated with these different types of transactions. The unique characteristics of international transactions include increased fraud risk compared to domestic transactions, chargeback processing, and increased complexities such as currency volatility. Accordingly, Visa asserts that the context of each transaction must be considered in assessing its value, and importantly, we would highlight that comparing 100 per cent domestic transactions with a network that processes both domestic *and* international transactions is not an appropriate like-for-like comparison.

2. Ensure there is commercial incentive for participants to bring security and innovation to the system

The value of the payments system, by nature, must maintain a level of equilibrium in order to thrive, and to grow. This essential balance between ensuring acceptance at a manageable cost, whilst encouraging investment in security, resiliency and innovation should be front of mind when considering regulatory interventions in payments. Otherwise, additional constraints on the economics of one or some payments providers will negatively influence their ability to compete effectively in the marketplace and reduce the economic incentives necessary to deliver new products and solutions as well as to maintain operational **resilience and risk and fraud mitigation** for consumers and businesses.

For example, the Australian payments industry has continued to investment in security and innovation since the regulatory changes regarding interchange compression enacted following the Reserve Bank of Australia's (RBA) 2015-2016 Card Payments Regulation Review. However, Visa has highlighted to the RBA that should the economics available within the payments system continue to be reduced, it could adversely impact the development of new services and competition as well as innovation (Visa (2020), p.8).

There are three areas where this is most important – for both the health of the payments system and for the protection and benefit of consumers and businesses – to ensure there are commercial incentives for continued investment: security, innovation and consumer experience.

Visa is committed to fortifying the **security** of both our network, and the broader payments environment to protect sensitive data, prevent fraud and to ensure the security and resiliency of the payments system and reliability of payment transactions. As the payments environment becomes more complex with constantly rising cyber threats, we are making ever greater investments to deliver the highest standards of security and cyber resiliency. For example, from 2015-2019, Visa invested nearly US$9 billion to enhance and secure our core technology platforms and launch new products and capabilities for system participants and our partners.

Responsible and secure **innovation** is essential for digital payments. Innovation not only enables new forms of payment but ensures the delivery of solutions designed to reduce risks across the system and to deter fraud. Visa encourages the New Zealand Government to continue its practice of fostering innovation in the digital payments system, and to ensure that networks can continue to compete in order to deliver the best technology to the country's consumers and businesses.

New Zealand's consumers and businesses have traditionally benefitted from innovation that delivers increasingly convenient methods of payment, enhancing overall **consumer experience**. Additionally, in an increasingly global commerce landscape, ensuring New Zealand businesses provide the experience expected by international consumers is key to attracting and retaining a global consumer base. As such, encouraging ongoing investment in consumer experience is essential, as is maintaining a consumer's right to choose the products and services that best meet their needs.

3. Ensure a level playing field

It is essential to ensure a level playing field among all participants, including incumbents (in New Zealand's case, EFTPOS, buy now pay later (BNPL) schemes and the international schemes) and newer entrants – both to balance the risks in the system as well as to maximise competition and innovation. For example, some participants in the payments system, such as

BNPL schemes, are not currently faced with the same regulatory requirements and, in some cases, their payment business is secondary to supporting expansion of their primary business lines. In other markets, where the playing field is tilted in favour of specific entities, or certain payment solutions, it has stifled competition – mainly to the detriment of local consumers, small businesses and domestic innovation. Overall, a level playing field is the best way to support New Zealand's ambition to advance innovation and growth in the payments system, and to ensure the economy remains digitally connected and globally competitive.

4. Understanding the unintended consequences of regulation

Before introducing regulation, it is essential to undertake scenario planning and explore whether there are any unintended consequences resulting from possible regulations. Regulators may seek to regulate interchange in order to reduce cost, address competition concerns and/or accelerate digitisation. However, regulation may not address these concerns and, instead, stifle the continued development of digital payments. To provide a specific example, Visa highlighted to the RBA the risk that smaller financial institutions (whether they are established credit unions or new fintechs) could be negatively affected by interchange reduction, including reduced competition leading to unintended consolidation of the sector.[5]

In this context, it is important to note that while regulation may seem like an approach to fulfill a policy objective of reducing merchant costs, there are other more effective alternatives that MBIE could consider. For example, it is innovation on the acquiring side, as well as investments in acceptance infrastructure, which lead to long-term, sustainable cost reductions for merchants – not interchange regulation. Additionally, Open Banking is likely to have a significant impact in encouraging new entities to enter the payments system in New Zealand which, in turn, will increase innovation and competition at all levels of the value chain. In fact, there are already new fintechs entering the system and providing, among other things, acquiring services that are driving down the costs of acceptance. This is likely just the beginning of new products, services, and business models that will emerge in New Zealand as Open Banking develops.

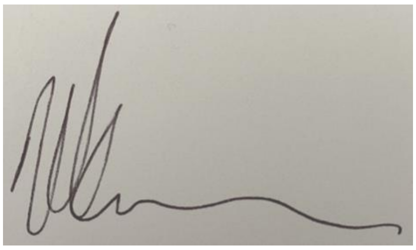
5. Taking account of New Zealand's unique dynamics

With amongst the highest digital payments usage globally, and an active local tech sector, New Zealand has unique dynamics important to consider in any regulatory review. Visa's experience is that while learnings should be sought from other geographies, replicating regulation inevitably does not take account of local circumstances and conditions and, therefore, can be detrimental. In addition, Visa notes that in determining interchange rates it considers the unique market conditions of specific countries as well as the value proposition of Visa's global network and technology and the need to drive innovation.

[5] Visa Inc (2020), "Response to the Reserve Bank of Australia's Review of Retail Payments Regulation Issues Paper", pp.26-27. ***https://rba.gov.au/payments-and-infrastructure/submissions/review-of-retail-payments-regulation/visa.pdf***

Visa welcomes that MBIE considers this part of the consultation as an initial opportunity to contribute, and that it will undertake a further round of stakeholder input. Given this openness to engagement, following MBIE's review of Visa's submission, I would appreciate the opportunity to discuss in more detail our perspectives on merchant service fee regulation. It would also be my pleasure to connect MBIE with Visa colleagues in other jurisdictions to discuss developments in other geographies.

Yours faithfully,



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Submission template

Regulating to reduce Merchant Service Fees

Your name and organisation

Name	[redacted]
Email	[redacted]
Organisation	[redacted]

[Double click on check boxes, then select 'checked' if you wish to select any of the following.]

☒ The Privacy Act 1993 applies to submissions. Please check the box if you do not wish your name or other personal information to be included in any information about submissions that MBIE may publish.

☐ MBIE intends to upload submissions received to MBIE's website at *www.mbie.govt.nz*. If you do not want your submission to be placed on our website, please check the box and type an explanation below.

I do not want my submission placed on MBIE's website because... [Insert text]

Please check if your submission contains confidential information:

☐ I would like my submission (or identified parts of my submission) to be kept confidential, and **have stated below** my reasons and grounds under the Official Information Act that I believe apply, for consideration by MBIE.

I would like my submission (or identified parts of my submission) to be kept confidential because... [Insert text]

1	**Do you have any feedback on our proposed approach to this project?**

Visa welcomes the opportunity to comment on this important topic, and appreciates the Ministry of Business, Innovation & Employment's (MBIE) efforts to engage with stakeholders in an open, clear and transparent manner. We are also encouraged that MBIE is considering this as an initial opportunity to contribute, and that it will once again undertake a further round of stakeholder input.

Our goal is to contribute to a robust and vibrant payments system in New Zealand, one that benefits all participants in the payments value chain. Merchant service and interchange fees are a key component to achieving that in a four-party, open loop network. When set optimally, they provide maximum value to consumers, businesses, and financial institutions.

In addition, critical to any review of the payments system is ensuring equal weighting is given to consumers and merchants. Focusing on one group over the other can upset the delicate system balance and have unintended and detrimental consequences.

2	**Have we described the retail payments system accurately? Is there any additional information that you would like to provide?**

The description of the New Zealand retail payments system is, in our view, broadly accurate, and it is critically important that the value delivered to consumers and businesses by the different models outlined in the Issues Paper is understood as central to the overall assessment of the system.

To ensure this value is recognised, we suggest considering the following areas as relevant to a holistic view of the payments system:

- **Investment in innovation:** In articulating the scheme role, it is important to include that Visa not only develops the technology and product features, as well as commercial and operational constructs, but also makes significant investments in these areas to enable financial institutions, merchants and third parties to deliver ongoing innovation to New Zealand consumers and businesses. Historically, these investments in innovation have included e-commerce, contactless, tokenised wallets such as ApplePay, and step up authentication (3DS). More recently, Visa's investment in technology and security protocols has enabled trials of new Tap-to-Phone technology benefitting New Zealand small businesses. Tap-to-Phone technology enables small businesses to turn their smartphone into a point-of-sale (POS) device.

  Investment in areas such as this is increasingly critical. The Issues Paper highlights the growth of digital wallets. While these are an important innovation in how New Zealand consumers conduct payments, they are only impactful because they effectively utilise a consumer's smartphone, allowing them to a more seamlessly and securely connect how they shop and pay.

The growth in mobile-based payments will continue as consumer expectations evolve and adjacent business models, such as subscription content services like Netflix and Spotify, set the bar for consumer experience. New Zealand small businesses will not be immune from this expectation and require significant investment in technology and security to bring the physical and digital worlds closer together through a mobile device.

- **The role of chargebacks:** Within the 'switch-to-acquirer' model, scheme system rules also facilitate the chargeback construct, which is of significant value to consumers and small businesses. Through this construct, consumers have the right to request a refund on a transaction that they believe was illegitimate or fraudulent. In this framework, businesses that utilise fraud management tools, such as 3D Secure, are similarly protected and not held liable for any illegitimate or fraudulent transactions that may implicate their business. The chargeback construct does not exist in the 'switch-to-issuer' model, further demonstrating the value produced, and therefore proportional cost, in the 'switch-to-acquirer' model.

- **Additional consumer protection, such as Visa's Zero Liability policy:** Visa's Zero Liability policy means consumers are not held responsible for fraudulent charges or unauthorised purchases made with their card or account information. Visa requires its system participants to provide Zero Liability as an important element in a trusted and secure payments system that benefits consumers and businesses.

- **Security and fraud management:** The 'switch-to-acquirer' model has a highly sophisticated level of security and fraud management inherently built in, which is becoming increasingly important as New Zealand businesses and consumers move online. To provide two examples:

  Artificial Intelligence: Visa has invested in Artificial Intelligence (AI) since the 1990s as part of its mission to make payments safer without introducing additional friction. Today, when a New Zealand consumer seeks to pay with their Visa card or other payment credential at a business in New Zealand or globally, Visa's Advanced Authorisation uses AI to analyse more than 500 risk attributes in approximately a millisecond and produces a score that reflects how risky the transaction is. The consumer's card or other payment credential issuer uses the score to decide whether to authorise or decline a given transaction and, at the same time, creates more confidence among consumers in digital payments. The fraud models continue to develop and refine as additional data points are included.

  Tokenisation: The industry, including Visa, has transformed the consumer experience and security of digital payments through tokenisation technology. Tokenisation protects a consumer's card or other payments credential details by providing a business with a highly encrypted token instead. While this technology is the most significant advancement in payment security for generations, it has also enabled a modern consumer experience in device and e-commerce payments. In addition, for e-commerce merchants, the ability to process recurring payments without needing to store consumer payment details removes significant business risk.

- **The setting of interchange:** Interchange is set in response to dynamic and highly competitive market forces and aims to strike an economic balance between all participants in the payments system. Among other things, interchange may vary by the type of merchant, cost of the sale, payment product type, processing technology and merchant use case. It is consistently monitored and adjusted in order to ensure that the economics and value of the transaction are balanced for all parties. If interchange is too low, then cardholders' financial institutions won't issue credentials; if interchange is too high, merchants won't accept them. Visa incorporates the broadest range of perspectives when evaluating interchange rates through bi-annual discussions with our payments system participants, businesses, and industry groups across retail, banking and payments; understanding the local competitive environment and value proposition for issuers, acquirers, cardholders and businesses is a cornerstone of successful interchange management. We continue to support MBIE regarding the transparency of interchange modifications and the average weighted interchange (AWI) for New Zealand. As covered further in our responses to Questions 3 and 22, interchange has been trending downwards in New Zealand.

3 Please provide information on your understanding of the levels of merchant service fees in New Zealand, any trends in relation to those fees, and how they compare to merchant service fees in overseas jurisdictions.

Each payment transaction carries a very different set of costs and delivers different value based upon several factors, including the card or credential type and the transaction amount, together with the types of risk and investment required to support different payment transaction types, including credit, debt, card-present, card-not-present, domestic, international, token, non-token, consumer, and commercial.

Whilst acquirers set merchant service fees, (for the avoidance of doubt, Visa is not privy to acquiring pricing), our market understanding is that in New Zealand merchant service fees can range from 0 per cent for the domestic debit system (EFTPOS), 0.65-0.7 per cent for Visa debit, and up to 3.5 per cent for credit card acceptance. Merchant service fees for BNPL platforms range between 4-6 per cent and up to 12 per cent for long-term retail finance products. New Zealand merchants' willingness to pay these fees depends, we understand, on their assessment of the value and choice in the digital payments system. Merchant service fees are dependent on the size and type of merchant, risk profile of the merchant, card present or card not present and whether the merchant prefers a fixed, bundled or interchange plus arrangement with their acquirer.

New entrant acquirers that offer full-stack services that include payment gateway solutions as well as acquiring (such as Stripe, Adyen, Worldpay, Checkout.com) are influencing the market as they bring new value in rapid merchant onboarding and specialisation in card not present facilities. In addition, payment facilitators like Shopify are making it easy for businesses to get online. The costs of new entrant services to businesses vary, with some being cheaper and some more costly than traditional acquirers. The growth in these services demonstrates the willingness of businesses to pay more for ease, speed or other such value. All acquirers have completed, or are about to complete, we understand, the unbundling of their merchant service fees for credit and debit transactions and increasing transparency on fees.

The payments system is a highly dynamic, evolving landscape. Visa constantly monitors the payments system to ensure that there are optimal levels of interchange in order to generate benefits for all participants across the payments value chain. As a result, actions we have taken in recent years have included reducing the Interchange Reimbursement Fees (IRF), which is a component of merchant service fees. In addition, we have undertaken consistent market reviews and the introduction of new programmes, such as the Contactless Fee Programme, to promote the use of innovations like contactless payments to help reduce merchants' cost of acceptance. In April 2018, Visa reduced IRF on contactless Platinum credit IRF by 20bps and again, in August 2020, we reduced IRF on all credit transactions by a further 20bps to help reduce merchant service fees. Additionally, Visa reduced debit IRF from 60bps to 30bps in 2014 and to 20bps in August 2020. Initiatives like these have seen merchant service fee reductions already taking place in the market, with the main bank acquirers now having fixed scheme debit merchant service fees at 0.65 per cent or 0.75 per cent.

For debit contactless acceptance, on an average weighted basis of 30bps as reported to MBIE, New Zealand is comparable to other regulated markets (Australia, the United Kingdom) and credit is higher at just over 1 per cent. But as a total weighted view, including the fee-free EFTPOS, the total AWI cost of acceptance in New Zealand is comparable to those markets as well.

4 What is your view on charges incurred by cardholders for the use of payment methods?

New Zealand's consumers choose to use methods of payment that provide them with the most value (for example, in terms of security and reliability), and in many cases, this value is equally important to a business. This dynamic is key to the success of payment networks around the world.

A key example of this is the provision of credit. Banks that issue credit cards to their customers are not only providing them with financial flexibility, but also financial security through a highly regulated instrument. These instruments are supported by significant customer behaviour monitoring and innovative financial management tools. Through this credit mechanism, businesses subsequently attract more consumers who have the financial capacity to purchase their goods or services. Another example of value delivered to both consumers and businesses can be seen in the degree to which businesses are willing to pay for BNPL services. As already mentioned, these products often cost more than traditional card products, but in some cases deliver increased sales – the lifeblood of any small business – while at the same time providing a segment of consumers with a different type of credit instrument that suits their lifestyle/preferences.

For these reasons, the cost and value equation for consumers' use of digital payments is complex. To say that consumers do not face the full cost of their choices presents a limited view that does not account for all groups, preferences and needs. Consumers pay relevant fees for different levels of value provided by a payment mode, and the protections and innovations that accompany it. This is part of the balance vital to a healthy, stable payments system and to which regulation that seeks to benefit only one audience can be damaging. For example, when merchant service fees were lowered following regulation in the UK, consumer fees increased.

In an increasingly fragmented and diverse consumer landscape, applying a general approach to the balancing of the payments system could be detrimental to the value delivered to all participants, consumers and businesses alike. Of utmost importance is allowing for choice and the ability of consumers and businesses to determine and select the products most valuable to their needs.

5 What impacts do you believe rewards and inducements have on the retail payments system?

In considering the impact of rewards and inducements on the retail payments system, it is important to note that to attract business, merchants compete by offering services that consumers wish to purchase. They can spend considerable resources in this regard, such as placing stores in convenient locations, offering free parking, maintaining attractive premises, advertising, and providing knowledgeable salespeople. The purpose of providing these services is to generate profitable incremental sales.

Each business determines whether a particular cost is justified based on the expected incremental sales generated. This kind of competition between businesses creates significant benefits for consumers. To the extent payment cards are a convenient way to pay and be paid, the costs associated with accepting cards should be seen as among the investments available to New Zealand merchants to increase sales (just as merchants who accept the relatively high cost/discount of accepting BNPL products have demonstrated on the basis that they drives incremental sales).

We also note that credit card-based reward programmes are similar to other merchant-subsidised programmes that encourage consumer loyalty. Other such programmes include Flybuys, AA Samart Fuel, Air NZ Airpoints programme to merchants-owned programmes like Countdown OneCard and Pak n Save Sticky Club. In MBIE's consideration of rewards programmes, a level playing field approach should be adopted, given the variety of rewards programmes in the market. Such an approach will ensure that competition regarding rewards unfolds on a level playing field – bringing with it benefits for both businesses and consumers.

Credit card-based reward programmes can be a highly effective way to enhance consumer loyalty. Businesses benefit from credit card reward programmes both directly and indirectly. These benefits include the ability to target marketing to members of reward programmes by offering discounts, additional rewards, and other inducements. Cards and other payments credentials that offer cash back or rewards redeemable for cash implicitly discount the price paid for goods, increasing demand for these implicitly discounted products and enabling consumers to save additional funds.

Consumers may decide to make additional purchases as a result of rewards promotions. As a result, businesses sell more goods, enabling them to keep prices low by absorbing the additional fees associated with card transactions involving rewards. While merchants' per-transaction net margins are reduced when they do this, their overall profits may remain the same or even increase due to the higher volume of transactions.

A study on the consequences of regulations designed to eliminate rewards and other inducements to consumers found that there is little chance that such policies produce benefits, while there is a large likelihood that they could prove detrimental to both consumers and businesses. It adds that payment networks have rules designed to ensure value creation across a wide variety and large number of transactions. While it may be possible to point to situations where, for a given transaction, some form of inefficiency may arise, that is to be expected. The study concludes that it is likely that such networks, given their extensive adoption, create widespread efficiencies and blunt regulatory intervention is likely harmful (Gans (2018), p.22).

In light of the rapidly evolving global payments market, in particular the predicted future growth of digital wallets, it is important to ensure a level playing field with non-card-based methods. Any lowering of the existing rates may shift consumer spending to unregulated players, including digital wallets and digital payment platforms. Additionally, because large e-commerce entities have full access to consumer transaction data, they are able to create robust consumer loyalty rewards and value-added services. However, because regulated interchange fees have impacted issuing banks' revenue streams, many have cut back on loyalty programmes, or have introduced card fees, which have in turn put card issuers at a distinct competitive disadvantage.

6

What is your view on charges incurred by merchants for the use (acceptance) of payment methods?

Analysing merchant service fees on a cost basis alone does not take account of all the value that digital payments provide to consumers, businesses, and financial institutions through security and value-added services. These benefits include savings already built in for businesses, including, among others, reducing the risks of, and time spent, handling cash and fraudulent cheques – see 'Costs of cash and cheques' below. The COVID-19 pandemic has also showcased the benefits for New Zealand's consumers and businesses of digital payments – enabling them to make purchases and sales despite lockdown. This is important for businesses in particular, given that in the three months to July 2020 most consumers were less likely to shop in stores and one in four shopped online more frequently (RFi Research (2020)).

This survey makes clear that the costs associated with accepting digital payments should be viewed as one of various investments available to businesses to increase sales. As stated in response to Question 5, in seeking to attract business, merchants compete by offering services and facilities that encourage consumers to make purchases. These can include stores in convenient locations, free parking, attractive premises, advertising, and knowledgeable salespeople. The purpose of providing these services is to generate profitable incremental sales. Each business determines whether a particular cost – including the costs associated with accepting digital payments - is justified by the expected incremental sales generated.

Businesses benefit from more consumers using digital payments in several ways. Firstly, for most purchases, cards and other payment credentials in general have lower total acceptance costs compared to alternatives (like cheques or cash). Secondly, businesses benefit from valuable computational and logistical services that other payment systems (such as cash and cheques) cannot replicate. For example, electronic records of transactions that are automatically created when a payment is made by card and other payment credential can simplify accounting. Thirdly, the growth of credit card usage by consumers and the commensurate growth of the digital payments industry have enabled more businesses to outsource their credit operations to banks. This has relieved them of the costs associated with fraud and expense as well as delays linked to operating in-house credit operations (see Layne-Farrar (2011) p.10, Zywicki (2000), p.111, Rochet and Wright (2009), p.24).

It should be noted that any immediate cost reductions for businesses from lower merchant service fees are not necessarily passed on to consumers (see Garces and Lutes (2018), p.31, Edgar, Dunn & Company (2020), p.31, Sarin (2019), p.4). In addition, these cost reductions often do not reach small businesses either. Regulators in Europe have acknowledged this in their review of the Interchange Fee Regulation (Edgar, Dunn & Company (2020), p.30) and similar conclusions have been reached in the United States (Sarin (2019), p.16). As a result, regulators should look at the long-term health of the digital payments system by balancing the costs and interests of all participants and not focus on certain constituents. For example, acquirer revenue from merchant service fees supports innovation and the creation of new products and services.

In the long term, acquirer innovation can have a greater impact on merchant cost savings than regulation. In addition to reducing costs, acquirer innovation grows card acceptance and the overall digital payments system. This creates more opportunities for businesses to generate sales and revenue. Today, there continues to be significant reliance on traditional POS and software, which is a significant factor in merchant acceptance costs. New entrants with pay-as-you-go (PAYG) solutions, using lower-cost mobile-based POS solutions, offer significant cost savings, particularly to small businesses.

Costs of cash and cheques

While a world with more digital payments means greater economic growth, security and convenience, for the foreseeable future there will be a role for cash alongside digital payments. Visa believes in consumer choice and will always support multiple payment options for consumers as well as businesses.

Nonetheless, the all-in costs of accepting cash and cheques are higher than the costs of accepting digital payments. According to the Association for Financial Professionals, the median cost of a cheque transaction is US$3, while costs associated with payments cards and other payment credentials are half that amount (Association for Financial Professionals (2015), p.1). Costs associated with cheques include printing, mailing, returned cheque handlinq, bank fees, and reissuance for lost cheques, among others.

For businesses in particular, cash is very expensive. The true costs of cash include bank fees, cash loss through internal and external theft, and transportation costs (e.g., armoured car transportation). Other costs include lost sales when a queue is long, and losing the opportunity to have better data on consumer preferences and trends.

A global study estimates that cash and cheques cost merchants US$0.07 in every dollar compared to US$0.05 for every dollar from digital sources (Visa (2017), p.4). A Bank of Canada study found that a cash transaction of C$20 costs a merchant C$0.48, compared to C$0.34 for a debit card transaction of the same amount (Kosse et al. (2017), p.22).

In 2020, Kiwibank stopped issuing and accepting cheques, citing that for the past five years the use of cheques at Kiwibank had been declining at a rate of 20 per cent year-on-year as customers chose less expensive ways to pay (Kiwibank (2020)).

The use of cash has also been widely shown to generate considerable economic costs to society, known as "social costs". Due to its physical nature, cash must be produced, stored, distributed and secured, which requires significant infrastructure. And, while useful in local face-to-face transactions, cash is extremely inconvenient for executing transactions with counterparties in remote locations or when conducting online and mobile commerce. Moreover, the ability of cash users to operate in the "shadow" economy hinders the ability of governments to fully implement desired fiscal and social policies and requires a disproportionate share of resources to identify tax evaders.

7	Please provide your views on barriers to merchants steering consumers to lower cost payment methods and the extent that steering occurs?

In Visa's view, consumer protection is a fundamental component of a healthy payments ecosystem. While there is currently no barrier in New Zealand to businesses being able to steer consumers to a certain payment type, steering results in the undermining of consumer choice and consumer protection. When a consumer makes a choice about which payment credential and payment network to use at the point of sale, a consumer has expectations with respect to levels of consumer protection, among other factors, associated with the transaction. When a business engages in steering, it essentially overrides the consumer's expectations about levels of consumer protection inherent in the transaction. For example, when a business advertises or represents that it accepts Visa payment credentials in order to encourage a sale, but then engages in steering, it results in invalidating the consumer's ability to fully benefit from the underlying protections Visa affords consumers. These include transaction, risk and security controls as well as dispute resolution processes, which provide assurances of integrity and legal certainty.

New Zealand businesses can choose from a range of payment methods – cash, domestic-issued EFTPOS cards, scheme debit, scheme credit and a number of high-level innovative products delivered through international schemes, such as contactless and mobile payments. In the growing e-commerce space, businesses also have multiple options, including debit, credit, PayPal, account to account, and BNPL. Along with the ability of businesses to determine the most appropriate payment methods based on the needs of their consumers, businesses can negotiate the level of service provided by an acquirer to process digital payments. These different service levels provide businesses a range of varied cost options, effectively allowing tailored approaches for their diverse needs.

While we naturally strive to ensure that businesses appreciate and accept the value Visa products offer, we recognise their right to choose whether to accept a Visa product or not, based on their business model and the impact to consumers who shop with them.

8	Please provide your views on the barriers to merchants surcharging and the extent that surcharging occurs?

Businesses can surcharge in New Zealand and in many cases do. This includes due to Visa agreeing, as part of an undertaking with the Commerce Commission in 2009, to not enforce our no-surcharge rule (Commerce Commission (2010)). Visa-commissioned research conducted in an independent capacity, undertaken by RFi Research, found that between August 2015 and August 2020 instances of New Zealand businesses passing on surcharges increased from 18 per cent to 37 per cent (of 500 card-accepting businesses surveyed). In that period, businesses operating in consumer services, professional services and manufacturing/construction were most likely to pass on a surcharge (RFi Research (2020)).

Businesses are more likely to indicate that they surcharge for credit than for debit and are also more likely to be intending to introduce surcharging on credit. Overall, most businesses agree that surcharging deters some consumers, however, businesses believe that consumers are more willing to accept a surcharge on credit card purchases. One third of the businesses who surcharge on credit believe that doing so does not deter consumers (RFi Research (2020)).

Part of the decision to surcharge is dependent on awareness and understanding of fees. The RFi Research survey showed that from August 2019 to August 2020, the proportion of businesses who agree that they have a good understanding of the level of fees paid for accepting various card payments and how they are charged those fees increased significantly (RFi Research (2020)).

Visa recognises surcharging in New Zealand as one of the choices available to businesses to manage their payments acceptance costs. But Visa maintains its global policy of opposing merchant surcharging as an inefficient disincentive for consumers to use digital payment products, effectively penalising consumers who use card payments and other payment credentials for a variety of reasons, including security.

Australia's experience has shown that allowing surcharging has, at times, led to profiteering by some businesses, i.e., through excessive surcharges above cost recovery. This has been particularly apparent in the airline and taxi industries. For more information, see the 'Australia Case Study' below.

In response to the argument that surcharging restricts higher pricing only to those consumers paying by cards or other payment credentials, a recent study found that maintaining the same price for all consumers regardless of payment choice helps achieve a level of digital payment usage that provides value to both businesses and consumers (Gans (2018), p.31).

Zero surcharging also promotes competition in the payments market and helps foster innovation as payments networks continue to strive to incentivise digital payments. Much of this innovation is centred on fraud-reduction and faster payments; this in turn makes digital payments safer and more convenient for consumers to use and for businesses to accept.

Australia Case Study

Following regulation in 2002, businesses in Australia were able to impose surcharges on payments made with credit cards. This included blended surcharging, which resulted in cheaper schemes subsidising higher-cost schemes and cheaper products (e.g., debit) subsidising higher-cost products (e.g., credit). However, most businesses did not introduce surcharges. While surcharging was not uniform, it was highly prevalent in areas where price discrimination and rent-seeking were profitable. Moreover, businesses almost ubiquitously imposed surcharges at rates that were considerably higher than the cost of acceptance: a RBA survey found that average surcharges in 2013 were 1.5 per cent of payment value, but because average merchant service fees were 0.8 per cent, this represented a nearly 90 per cent markup over the merchant service charge (MSC) (see Stillman et al. (2008), pp.25–26, citing survey evidence from 2004–07 indicating that surcharges ranged from 15bps to 81bps higher than the MSC). Clearly, businesses had used surcharging as a means of price discrimination against consumers using credit cards.

To remedy this, on 25 February 2016 the Competition and Consumer Amendment (Payment Surcharges) Act 2016 became law. It inserted a new part into the Competition and Consumer Act banning excessive payment surcharges and provided new powers for the Australian Competition and Consumer Commission to investigate consumer complaints and take enforcement action where necessary. While this remedial action was welcomed, in Australia at present there is a need for a level playing field regarding surcharging. For example, most BNPL providers have rules that prevent businesses from levying a surcharge on consumers. This matter is currently under consideration as part of the RBA Review of Retail Payments Regulation (Reserve Bank of Australia (2020)).

9 What is your view of the wealth transfer by merchants passing on merchant service fees in the price of goods and services to all their consumers?

There are several international examples where interchange regulation has been introduced and has seen unintended consequences for consumers. This includes little or no pass through of merchant service fee savings for consumers. Below are a few examples:

Australia

Regulation in Australia appears to have brought about redistributions in income and welfare rather than welfare gain, with some parties (merchants) gaining and others (financial institutions and ultimately consumers) losing (Garces and Lutes (2018), p.30). In fact, there is little empirical evidence of pass through of savings in the form of lower prices offered to consumers.

Europe

Research indicates that acquirers in Europe have passed on a proportion of the interchange reduction, but this has largely benefited mega and large businesses. In this case, there is limited evidence of merchant pass through to consumers (Edgar, Dunn & Company (2020), p.30). The European Commission itself issued similar findings recently in its review of the Interchange Fee Regulation (European Commission (2020), p.14, p.87). More specifically, the annual decline in the merchant service fees (or what is known in Europe as the merchant discount rate) is estimated to be around €1,200 million, while the annual interchange revenue of banks declined €2,680 million.

United States

Studies have shown that the Durbin Amendment, which mandated a regulation aimed at reducing debit card interchange rates and increasing competition in the payments industry, harmed consumers not only because banks increased consumer account fees to recover lost interchange revenue, but because businesses failed to pass through cost savings to consumers and, in some cases, raised prices (Sarin (2019), p.4). For the debit interchange regulation to benefit consumers, businesses would need to pass savings to the consumer in the form of lower prices. One study concludes that when regulators restrict non-salient fees (i.e., fees not readily perceived by the average consumer) – as these interventions did – businesses are unlikely to pass the costs through to consumers (Sarin (2019), p.5).

10 What barriers do small businesses face to obtaining competitive merchant service fees?

There are several factors that contribute to a merchant's ability to ensure the most efficient merchant service fees for their business. New Zealand is a competitive market for merchant acquiring, with the major banks offering merchant services to retain and win transactional business accounts. Additionally, there are a number of newer entrants to the market providing discreet, standalone acquiring services. Often these acquirers serve a segment of the business community quite different from that traditionally served by banks. For example, businesses who want to expand into the online and digital marketplace and need a single online integrated platform or compatibility with a range of international currencies.

Businesses should actively engage with their acquirer and review other offers available to them (including via a competitive pitch process). Some of the other options available to businesses can also reduce their overall costs, for example, by insisting on unbundled pricing and in certain cases by surcharging at a level appropriate to but not exceeding incremental cost.

One potential barrier for small businesses is their lack of awareness and education of what is available when they decide their acquirer and the payment solution that best suits their needs. That said, in certain cases, businesses value the convenience of a bundled price, which provides price certainty and does not require resources to manage the cost of merchant service fees. In addition, some businesses are not exercising their options because they choose to focus on other business priorities.

11	**What information or assistance would assist small business to obtain better deals?**
	Visa supports transparency in the cost of retail payments, and we believe all participants in the payments system have an important role to play in enabling this. From a scheme perspective, Visa publishes maximum domestic interchange rates applicable in New Zealand on Visa's local website (www.visa.co.nz) and has done so for a number of years. Issuers list their individualised rates on their websites. It is important that small businesses have clear, accurate and consistent information available to them from their main bank, other banks, non-bank acquirers, payment gateways, terminal providers and industry bodies, such as Retail NZ and Payments NZ, when they are reviewing payment solutions and their costs of acceptance. Visa works with these industry participants and our payments system participants to provide clear and consistent information that can be shared with businesses and industry groups alike to promote awareness and understanding of the digital payments system.
12	**What cost differences are there for providing merchant services to small businesses compared with larger businesses?**
	The payments system by its very nature must maintain a level of equilibrium in order for it to thrive and grow. There is almost always a difference in the merchant service fees that large and small businesses pay. Acquirers set their merchant service fees taking into account a number of factors, including merchant volume, merchant category, average ticket size, and payment channel (face to face, online or card on file). Therefore, the reason there are different price points is because varying market forces drive different servicing cost, risk and benefits associated with small businesses compared to large merchants. Small businesses need to be individually managed and have similar servicing requirements to large merchants regarding authorisation, clearing and settlement of funds as well daily/monthly billing reports, fraud protection, risk and chargeback-related services - without the scale to apportion these costs. New to market and small businesses have limited financial and transaction history and an acquirer can be at a greater risk to guarantee their transaction payment volume. Separately, there are a range of interchange rates available for businesses in New Zealand. These are applicable to both face-to-face and online businesses. The rates are publicly available and range across categories, including industry, and category rates for charity, recurring, utility, insurance, government, strategic merchants, product debit and credit rates.

13 How much competitive discipline does EFTPOS provide on scheme debit card merchant service fees and are there any barriers to domestic EFTPOS providing more competitive discipline on merchant service fees?

As EFTPOS is subsidised to a zero cost of acceptance for businesses, it is not a like-for-like comparison to scheme debit in terms of merchant service fees. The true cost of providing this service is not borne by either businesses or consumers. More importantly, EFTPOS' limited product features make it infeasible as the main payment option for a growing number of consumers and businesses who require contactless, e-commerce, and/or overseas transaction capabilities.

Notwithstanding these important differences, EFTPOS affects significant competitive discipline on scheme debit domestic card present transactions. Visa estimates that one in five New Zealand businesses do not accept any Visa products. We further estimate that of the four in five businesses that accept Visa, one in three do not accept contactless payments.

The proportion of businesses that do not accept Visa at all has remained relatively consistent over the past few years. The proportion of businesses that do not accept contactless has declined over the past few years. It is among this group of businesses that EFTPOS has exerted competitive discipline. That is, to open up broader acceptance for contactless in New Zealand, the cost of acceptance has reduced significantly, both in terms of interchange and merchant service fees.

As acquirers unbundle their merchant service fees for scheme debit, the delta to EFTPOS and scheme debit is smaller. The main bank acquirers now have fixed scheme debit merchant service fees at 0.65 per cent or 0.75 per cent - even less if the business is on an interchange+ pricing model.

EFTPOS has operated in a similar fashion since it was introduced to address the use of cash and cheque. Operating under a fundamentally different model to scheme debit, businesses pay for EFTPOS payments via a monthly license fee and, as such, have demonstrated there is value in the service. The service, however, has not invested in innovation in the face of the ever-changing payments landscape – such as the move from mag stripe to EMV, e-commerce, contactless payments and advanced fraud-fighting capabilities that protect consumers and businesses alike.

Visa invests heavily in its network to ensure those in the four-party model have access to secure, convenient and ubiquitous payment methods. Issuers have made an active choice, as have acquirers and businesses, to offer and accept these payments based on the value provided to the participants. Visa continues to invest in innovation, ensuring that the ongoing security and ease of commerce provides consumers and businesses with payment mechanisms that meet their needs. Comparisons in transaction costs for very different network propositions do not truly assess the value that international schemes can deliver. This value is provided throughout the payment network, whether it be enhanced platform services, including fraud detection,

protection for issuers, acquirers and businesses, analytical capabilities for businesses or the convenience to consumers of instore, online or overseas payments.

14	What impact is product innovation having on merchant service fees?

Analysing merchant service fees solely on a cost basis does not take account of all the benefits that digital payments provide to businesses, including increased security and value-added services. That is:

- The long-term trend away from purely cash acceptance toward more mobile and digital commerce, which has been dramatically and permanently accelerated during the pandemic.
- The savings already built in for businesses, including, among others, from not having to manage risks and time spent handling cash.
- Economic literature has shown evidence that any immediate cost reductions for businesses from lower fees are not necessarily passed on to consumers (Garces and Lutes (2018), p.30).
- Regulators should focus on the long-term health of the payment system by balancing the costs and interests of all participants rather than certain constituents.
- Acquirers need adequate profit margins in order to invest in new acceptance at smaller businesses.

In addition, long-term and sustainable cost reductions for businesses stem from innovation on the acquiring side, which are particularly beneficial for small businesses. Specifically:

- Acquirer revenue from fees supports innovation and the creation of new products and services. In the long term, acquirer innovation can have a greater impact on merchant cost savings than regulation.
- In addition to reducing costs, acquirer innovation grows card acceptance and the digital payments system. This creates more opportunities for businesses to generate sales and revenue.
- Today, there continues to be strong reliance on traditional POS and software, which is a significant factor in merchant acceptance costs. New entrants offering pay-as-you-go (PAYG) solutions, using lower-cost, mobile-based POS solutions (such as Tap to Phone), offer significant cost savings, particularly to small businesses.

As seen in other markets, such as the United Kingdom, United States and Australia, innovation is less about the entry of new payment schemes and more about the entry of new payments participants and their propositions for the end customer, whether that customer be a business or consumer.

As an open network, Visa's network technology innovations and licencing programmes enable a variety of existing payments providers and new entrants to launch propositions that deliver new consumer experiences quickly and securely. For example, in Australia, BNPL provider, Zip, partnered with Visa to enable consumers to set up a virtual card for their Zip account, which can then be used to tap and pay anywhere contactless payments are accepted. This additional capability provides face-to-face businesses with access to even more consumers, without having to sign up for a BNPL service and the fees associated with this.

Similarly, from a payment acceptance perspective, Visa's open network has allowed new acquirers and payment gateways to enter the market and drive competition in the online commerce environment. For example, entities such as Adyen and Stripe provide a broad range of services and capabilities to help small businesses make the transition to online. These new entrants have been successful in the e-commerce environment, as this allows for more seamless integration comparative to the face-to-face switch-to-issuer domestic debit system in New Zealand.

In Visa's experience, the companies that drive innovation in payments focus on security, ease of integration, flexibility and speed. This competition set requires such basic scheme tenets to make their business models viable, deliver value to their end consumer and meaningfully compete in the local market.

15 Is open banking likely to provide sufficient competitive discipline on scheme debt and credit fees?

Visa commends MBIE for working with industry as it considers the most appropriate data-sharing model for the country's businesses and community. Open Banking has the potential to create and deliver innovative financial products and services, in addition to traditional banking services, that may not otherwise be available to a significant number of New Zealand consumers and micro-, small-, and medium-sized businesses. As Visa noted in our submission to MBIE in October 2020, we believe that an Open Banking model should be guided by the following principles:

- A flexible and principles-based consumer data-sharing model;
- Inclusion of diverse payments system participants;
- Intermediaries as drivers of value, security, and efficiency;
- Commercial incentives to ensure continued investment in the payments system;
- Interoperable, consumer-focused Application Programming Interfaces (APIs);
- Empowering consumers to manage their data;
- Data sharing as a catalyst for inclusion and information equality; and
- Representative governance.

Open Banking is likely to have a significant impact in encouraging new participants to enter the payments system in New Zealand which, in turn, will increase innovation and competition at all levels of the value chain. In fact, there are already new fintechs and enablers entering the system and providing, among other things, acquiring services that are driving down the costs of acceptance. This is likely just the beginning of new products, services, and business models that will emerge in New Zealand as Open Banking develops. As such, given that New Zealand is still in the early stages of developing a data-sharing framework, we encourage MBIE to allow Open Banking

	to properly develop and deliver benefits to all participants in the payments system before it proceeds to pricing regulation. In fact, proceeding to regulation before enabling innovation to flourish is not in alignment with how New Zealand has otherwise approached payments system development, oversight, and regulation.
16	Do you agree that there is a gap in regulatory governance of the retail payments system relating to promoting competition and outcomes that are in the long-term benefits of end-users?
	We do not believe there is a gap in the regulatory governance of the retail payments system. In our view, market forces will continue to drive competition and outcomes that will benefit end users over the long term. For example, Visa has for three years voluntarily provided half-yearly interchange reporting to MBIE on contactless credit and debit as well as card not present debit. This reporting has shown a progressive decline in interchange, and we would welcome further dialogue with MBIE on how best to sustain this trend in a way that maximises and optimises digital payments adoption across the entire economy.
18	Do you agree with the objectives for the retail payments system in New Zealand?
	Visa broadly agrees with the objectives for the retail payments system that have been set out in the Issues Paper - in particular, the need to incentivise beneficial innovation. Without the technical and commercial structures to support investment in payments system innovation, it will be difficult to meaningfully achieve the other objectives identified in the Issues Paper. For example, competition would not exist if payment providers delivering consumer and business choice do not see a return on the investment required to participate. Similarly, innovation allows for new business models to be created that have the appropriate price structures for that segment. For example, Tap-to-Phone technology removes the cost of hardware for small and micro businesses. In relation to the role of the Reserve Bank of New Zealand in governing security and reliability of the payments system, it should be noted that investment in innovation is what ensures the security and reliability of the system. For example, tokenisation technology creates valuable digital payments experiences, but also ensures security. Creating excessive separation in these roles should be carefully considered.
19	Please provide feedback on the aspects of the proposal for interchange regulation, including any changes that would improve the impact of it, with supporting evidence of any benefits or costs.
	Visa notes with concern that MBIE is considering interchange fee regulation in an effort to reduce merchant service fees, because we believe this approach may do more harm than good for New Zealand consumers and merchants, especially small businesses. The frequently cited assumption that fee regulation helps to drive down payment costs ignores the fact that price ceilings inevitably reduce the total pool of available resources for investment and innovation in the payments system. With digital technology evolving faster than ever before, the consumer landscape is changing rapidly. Considering all of these current trends, introducing price controls

for payments now would create unnecessary risks just as the New Zealand economy is on the cusp of launching into long-term recovery.

It is important to recognise that New Zealand has had enormous success in growing digital payments over many years. According to RFi Consulting (2014), New Zealand has one of the highest penetrations of digital payments in the world. This success was achieved on the basis of strong free market principles. This was important in the pre-COVID-19 world. But it is even more so in the context of COVID-19 and beyond, as digital payments have supported the shift from an 'in person' world to a 'virtual' world, enabling consumers to buy safely and businesses to continue selling, all while ensuring safety, security and resiliency of payments. As a result, we strongly encourage MBIE to carefully consider the policy outcomes that an intervention – particularly at this volatile time - might lead to.

On interchange regulation, it is important to note the complexities associated with the process of determining interchange rates. The process considers the unique market conditions of the relevant country/ies, the need to encourage continuous investment in innovation and security, and the value proposition of Visa's global network and technology. In Visa's view, this undertaking is most effective when it is market-led. In setting optimal interchange rates, our goal is to grow the two-sided market and encourage consumers to adopt and use cards and other payment credentials, and merchants to accept them.

Global experience and economic research indicate that regulation is not necessarily effective in accomplishing these goals and may even have the opposite result (Hugo-Webb (2013), pp.1-23). For example, a review of several jurisdictions that have implemented interchange regulation demonstrates that while some businesses may receive some cost reduction and savings from their acquirer contracts, these savings were not necessarily passed on to consumers or have not resulted in lower product prices (as we outlined in more detail in response to Question 9). The research also indicates that in countries where interchange regulation has been enacted, there has been an increase in cardholders' fees and a reduction in benefits. Lower interchange fees have also resulted in reduced revenue for issuers, which, in turn, may negatively impact the broader system. With acquirers, lower revenue discourages them from initiating new acceptance at smaller businesses (Hugo-Webb (2013), pp.1-23).

20 Please provide feedback on which body or bodies would be best placed to act as the regulator for interchange fee regulation.

Given Visa's experience across 200 markets, in responding to this question we focus on the best practices regarding flexible regulatory frameworks for digital payments systems rather than concentrating on which body or bodies in New Zealand are best placed to act as the regulator for interchange fee regulation. This approach is designed to enable MBIE to assess what attributes a regulator should possess and the approaches it is best recommended to adopt in building and maintaining a vibrant digital payments system.

In considering the most suitable regulatory architecture, Visa recommends that in addition to the principles outlined in our cover letter a technology- and sector-neutral approach is most beneficial. In this regard, the regulatory framework should be flexible enough to encourage innovation and allow different technologies and business models to emerge across all levels of the value chain, whilst at the same time ensuring a level playing field for competition across a growing range of services. In short, the goal should be to maintain a level playing field without removing incentives for innovation.

In order to create a level playing field, there is value in regulatory bodies considering whether regulation is required as well as the scope of any overarching regulation being focused more on the nature of services provided rather than the form of organisations providing them.

More specifically, we recommend a flexible regulatory architecture that possesses the following attributes, and which adopts certain approaches - rather than an overly prescriptive, top-down regulatory approach that is unlikely to support variety and speed in innovation:

- In taking into consideration the payments environment as it is today and what it may look like in future, the regulatory architecture should be centred on supporting innovation in products, services, security, resilience and new entrants as well as ensuring the vibrancy and competitiveness of the payments system.
- Policy settings should be designed to take account of the economic incentives necessary to deliver new products and solutions, mitigate risk/fraud for consumers, and not disproportionately advantage one party over others.
- Systems and policies should be in place to ensure the independence of decision-making and governance through the removal of any conflicts of interest – for example, when regulators also own or operate payments system infrastructure. Otherwise, there is the risk of disrupting the level playing field within the payments system.
- A flexible framework based on robust two-way engagement, consultation and coordination among industry participants and regulatory bodies. This ensures that policy-making is collaborative, adequately reflects marketplace dynamics, is sufficiently flexible to adapt to new technological developments, and can accommodate a variety of business models and commercial incentives.

Beyond these specifics, Visa has found that the most appropriate framework for supporting payments innovation is a multi-faceted regulatory regime in which regulators have clear responsibilities based on their respective legislative authorities and areas of greatest policy expertise, as well as relevant analytical and enforcement capabilities. Coordination across regulatory bodies, not consolidation, leads to some of the most innovative policy initiatives.

21	**Please provide your views on the impacts of the above classes of options, with supporting evidence of the benefits and costs.**
	In Visa's assessment, formal regulation of the payments system would do more harm than good for New Zealand consumers and merchants, especially small businesses. Interchange or any form of other price regulation would create economic distortions and reduce overall value to the national economy. Furthermore, there would be negative impacts to New Zealand's global competitiveness with respect to technology, innovation, and the ability to attract new investment. This position is based on the clear benefits resulting from the steady growth of digital payments in New Zealand as well as the unintended consequences that could arise from potential regulation. On the specific options identified in the Issues Paper, Visa believes it is beneficial for New Zealand businesses to understand the costs of acceptance, particularly a scheme debit contactless transaction versus a scheme credit transaction. In this regard, we support a transparent approach. Easily accessible transparent merchant service fee information would give businesses the ability to financially assess the individual payment methods they wish to offer. This move would also support a naturally competitive environment that ensures schemes, acquirers and issuers provide consumers with an economic proposition that drives adoption and acceptance.
22	**Please provide your views on any other feasible options that should be considered, with supporting evidence of the benefits and costs of these options.**
	Visa believes that leveraging an industry-led, self-regulatory model and continued close consultation with government will support a sustainable, secure and interoperable payments system in New Zealand. As the Issues Paper describes in section 105, steps taken by Payments NZ, the schemes and the banks to date have led to improvements. For example and as already outlined, Visa has proactively reduced interchange and pricing in New Zealand as a result of government-industry engagement. Ongoing constructive engagement with government and industry will continue to deliver a sustainable, secure and interoperable payments system – without a potentially lengthy regulation process, implementation, additional regulatory responsibility for a government/regulatory agency, and the unintended consequences cited in this response.

Other Comments

ABOUT VISA

Visa is the world's leader in electronic payments. Our mission is to connect the world through the most secure, reliable and innovative payment network – enabling individuals, businesses and economies to thrive. Our advanced global processing network, VisaNet, provides secure and reliable payments around the world, and is capable of handling more than 65,000 transaction messages a second.

In New Zealand, Visa has a physical presence in Auckland. Together with our broad range of partners and payments system participants, from New Zealand financial institutions, merchants, fintech and technology companies, we are committed to building a future of commerce that fosters New Zealand's economic growth and innovation.

Visa also has made investments into New Zealand, with a 100 per cent owned subsidiary, Fraedom Inc., a leading software-as-a-service technology company providing payments and transaction management solutions for financial institutions and their corporate customers. Starting in New Zealand as one of the original fintech start-ups over 20 years ago, today Fraedom is headquartered in Auckland and has a team of close to 350 people delivering transaction management products and services, including expense management and accounts payable solutions to 600,000 organisations in 178 countries.

Fraedom and Visa share a vision for enabling big and small businesses to thrive with solutions that add convenience and security to everyday life, and Visa's acquisition of Fraedom is a good example of our commitment to invest in New Zealand. The two companies are also aligned in our focus on diversity of talent and are committed to empowering and advancing New Zealand talent.

Supporting New Zealand small- and medium-sized businesses is at the heart of Visa's mission to enable individuals, merchants and economies to thrive. Launched in June 2020, Visa's Where You Shop Matters initiative promotes New Zealand small businesses and helps to enable them for e-commerce, providing access to an increasingly online consumer base, including Visa's global cardholders. Last year, these cardholders made 140.8 billion transactions, each of them benefiting businesses and helping local economies to grow.

As the trend toward digital payments continue, enabling innovation and entrepreneurship is a key focus for our business in New Zealand. In 2020, Visa saw a rapid acceleration of several payment trends in key areas, such as e-commerce, digital wallets, peer-to-peer payments and instalment solutions, among others. We recently:

- Launched our fintech accelerator programme in New Zealand and across the Asia Pacific

- Announced Tap to Phone, an emerging technology that can provide New Zealand retailers with an innovative payments acceptance solution using their smart phone at the point of sale
- Rolled out Click to Pay, a new, simple and secure way to shop online
- Worked closely with the broader payments system to ensure security remained at the forefront of any innovation through industry standards and initiatives, such as Visa's *Future of Security Roadmap* and *Biometrics* report launched in 2019 and 2020 respectively.

As an active member in New Zealand's business community, Visa works closely with Retail NZ, Payments NZ and the New Zealand Bankers Association, with regular consultation on matters relating to the New Zealand payments system. In technology, Visa supports the prestigious Hi-Tech Awards in the category of Best Hi-Tech Solution for Public Good. Additionally, we are a member of Digital Identity NZ and Fintech NZ and contribute to these industry groupings, especially through our global experience and perspectives.

To learn more, visit ***www.visa.co.nz***

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