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Application to the ACCC for the proposed amalgamation of BPAY, eftpos and NPPA

Mastercard response to the proposed undertaking

August 2021

1. Executive summary

1.1 This submission is made by Mastercard in response to the request by the Australian Competition and Consumer Commission (**ACCC**) in its letter dated 6 August 2021 (**Letter re Proposed Undertaking**) for comments from interested parties on whether the undertakings attached as Schedule A to the Letter re Proposed Undertaking (**Proposed Undertaking**) addresses the competition concerns arising from the Application to the ACCC by the Industry Committee, on behalf of its members who are shareholders and/or members of BPAY, eftpos and/or NPPA, to amalgamate under AP+ (formerly referred to as NewCo) dated 18 March 2021 (**Application**)[1].

1.2 For the reasons set out below, and with reference to Mastercard's April 2021 submission (**Mastercard's First Submission**) and Mastercard's June 2021 submission (**Mastercard's Second Submission**), together with the reports by Oxera, Mastercard:

(a) notes that the premise underlying the rationale for LCR, namely that “many merchants incur higher fees transactions [processed through the Debit Mastercard scheme] than those processed through eftpos”, is incorrect as:

(i) Mastercard does not levy fees to merchants, the merchant’s acquirer (or payment facilitator) determines the Merchant Service Fee that it will charge merchants for Mastercard DNDC transactions processed by either eftpos or Mastercard; and

(ii) consistent with consumer protection including the right of choice where outcomes potentially go to the risk of fraud, the potential savings associated with LCR are frequently overstated and based off data that does not enable like-for-like comparisons.

(b) asserts that consumers should be informed and have the ability to choose how their DNDC is being routed.

(c) notes that the Proposed Undertaking potentially raises additional competition concerns, especially if the undertakings and the mandates therein have the potential to effectively foreclose competition from superior products, services or capabilities offered by third parties, or act as a deterrent to implement and utilising these superior products, services or capabilities of third parties, including Mastercard.

(d) highlights that despite Mastercard and other interested parties highlighting access issues that could present barriers to entry for new participants and/or foreclosure risks, in particular with respect to the NPP, this has not been addressed in the Proposed Undertaking.

2. Introduction

2.1 In its letter accompanying the Proposed Undertaking, the ACCC states that[2]:

(a) the Proposed Undertaking seeks to address the ACCC’s competition concern that the proposed amalgamation may result in the major banks or AP+ reducing support for eftpos and a decrease in the availability of least-cost routing (**LCR**);

(b) LCR is a functionality that allows merchants to choose which debit card scheme will process payments made by consumers using dual network debit cards (**DNDCs**). Without LCR, DNDC transactions would typically only be processed through the Visa

[1] Terms used in this submission that are not otherwise defined herein have the same meanings as defined in the Letter re Proposed Undertaking or Application (as the case may be).
[2] See page 1 of the Letter re Proposed Undertaking

Debit or Debit Mastercard schemes, which for many merchants incur higher fees transactions than those processed through eftpos; and

(c) if the support for eftpos was reduced and the availability of LCR was decreased by the major banks or AP+ as a result of the merger, it could reduce eftpos' ability to compete with Visa and Mastercard and, consequently, there is a risk that the amalgamation may substantially lessen competition in the routing of debit card payments.

2.2 It will be for the ACCC to assess whether the Proposed Undertaking addresses the ACCC's competition concern noted in 2.1 above. In this submission, Mastercard instead focuses on:

(a) least cost routing;

(b) the potential for undertakings and/or mandates in the Proposed Undertaking to have anti-competitive purpose or effect; and

(c) foreclosure risks and access to the NPP infrastructure.

3. Least Cost Routing

3.1 In analysing the submissions made by interested parties, it was evident that a number of interested parties, especially those representing small business organisations, view eftpos as a competitive wedge in the Australian payments market.

3.2 Mastercard believes in competition, it drives innovation, best solutions and best pricing. However, Mastercard notes that the premise underlying the rationale for LCR, namely that "many merchants incur higher fees transactions [processed through the Debit Mastercard scheme] than those processed through eftpos", is incorrect as:

(a) Mastercard does not levy fees to merchants, the merchant's acquirer (or payment facilitator) determines the Merchant Service Fee[3] that it will charge merchants for Mastercard DNDC transactions processed by either eftpos or Mastercard; and

(b) consistent with consumer protection including the right of choice where outcomes potentially go to the risk of fraud, the potential savings associated with LCR are frequently overstated and based off data that does not enable like-for-like comparisons.

3.3 We refer below to the limitations associated in the current RBA data which is commonly used as the basis for comparing payment scheme costs highlighted by the Australian Banking Association's (**ABA**), as well as analysis indicating that the price impact for small merchants who use LCR is unlikely to be material.

Merchant Service Fees

3.4 Mastercard does not issue cards, extend credit, determine or receive revenue from interest rates or other fees charged to account holders by issuers, or establish the rates charged by acquirers in connection with merchants' acceptance of our products. In most cases, account holder relationships belong to, and are managed by, our financial institution customers. We generate revenues from assessing our customers based on the gross dollar volume (GDV) of

[3] The RBA released its Consultation Paper on the Review of Retail Payments Regulation in May 2021 (**Consultation Paper**) in which it defines a **Merchant Service Fee** as a transaction-based fee (or a time-period-based fee that covers a specified or maximum number of transactions) charged to a Merchant by an Acquirer for Acquiring, or by a Payment Facilitator for arranging the Acquisition of, one or more types of Card Transaction from that Merchant whether collected on an ad valorem or flat-fee basis, or charged as a blended or bundled rate across more than one type of Card Transaction or on an interchange plus acquirer margin basis or any other basis.

activity on the products that carry our brands, from the fees we charge to our customers for providing transaction switching and from other payment-related products and services.[4]

3.5 It is the merchant's acquirer (or payment facilitator) that determines the Merchant Service Fee that the merchant will pay on a Debit Mastercard transaction. In Mastercard's response to the Reserve Bank of Australia's (**RBA**) Review of Retail Payments Regulation Consultation Paper, we highlighted that[5]:

(a) the use of blended/blended fees for the international card schemes obscures the actual costs for different card transactions and sends distorted signals as to the costs of different payment schemes; and

(b) merchant routing decisions should be made based on value and not cost alone, and that unless and until all acquirers:

(i) price Mastercard transactions based on actual Mastercard fees;

(ii) cease bundling pricing for Mastercard with Visa (and/or other international schemes including China Union Pay, Discover, JCB and American Express) and across different transaction and card types, including card present/card not present, debit/credit and domestic/international; and

(iii) enable dynamic routing to the lowest cost payment scheme,

"Merchant Choice Routing" or "MCR" should be the term used by the RBA and all industry participants to describe such routing, and not "Least Cost Routing" or "LCR".

3.6 As it is the merchant's acquirer (or payment facilitator) that routes a Debit Mastercard transaction to either Mastercard or eftpos, as well as determines the Merchant Service Fees payable by that merchant for a transaction routed to Mastercard or eftpos, whether a merchant benefits from LCR is within the hands of that acquirer (or payment facilitator). We leave it to the ACCC to assess whether the Proposed Undertaking addresses the ACCC's competition concerns, but we would query whether having the Proposed Undertaking coming from AP+ as opposed to each Applicant that operates as an acquirer (or payment facilitator), and who are the organisations that offer/enable LCR, is sufficient to address these.

LCR 'Savings'

3.7 The RBA's merchant fees data report (*RBA Table C3: Average Merchant Fees for Debit, Credit and Charge Cards)* is commonly used by industry participants such as eftpos, the RBA itself, industry commentators and others as a basis for comparing payment scheme costs.

3.8 The ABA in its submission to the ACCC dated 18 May 2021 (**ABA Submission**) highlighted some of the limitations associated in the current RBA data, in particular that:

> *"the current merchant fee data the RBA receives and uses in this report from banks is not comparing 'apples with apples'. This is because the current RBA data collection compares fees charged for routing face-to-face domestic debit transactions via the domestic eftpos network with international networks fees, which are reported as a combination of domestic debit transactions, international card holders' domestic debit transactions and e-commerce transactions."*[6]

3.9 As noted in Mastercard's submissions to the RBA on its Review of Retail Payments Regulation, data analysed so far shows the price impact for small merchants who use LCR is

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[4] Mastercard refers to 2.3 and 2.4 of Mastercard's First Submission.
[5] Mastercard refers to pages 14, 19 and 20 of its submission, https://www.rba.gov.au/payments-and-infrastructure/submissions/review-of-retail-payments-regulation-may-2021/mastercard-2021-07-09.pdf
[6] See page 3.

unlikely to be material. According to research commissioned by Mastercard[7], a typical small merchant might handle $500,000 of card payments per year. A 0.1 percent (10 basis points) saving on acquiring costs would generate savings to a merchant of about $42 per month.

3.10 One industry participant suggests a shift to LCR could save merchants an average of 8.5% on their Merchant Service Fee, with savings varying between merchants and depending on a range of factors[8]. So, based on the RBA's average merchant cost of 0.46% for debit, on the sale of a $3.50 cup of coffee a merchant will save on average $0.00137 in merchant service fees per transaction. On a $10 transaction a merchant will save $0.00391 and on a $20 transaction they will save $0.00782.

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3.13 Potential merchant savings associated with LCR, and by routing Debit Mastercard (and Visa Debit) DNDC transactions to eftpos, have been spruiked to run to hundreds of millions of dollars based off this RBA data. However, the ABA concluded that the "cost savings currently being cited by submissions should be treated cautiously".[9] As evidenced above, savings merchants make through LCR are minimal and unlikely to translate into lower consumer prices.

3.14 Should the transaction be compromised, and fraud occur, the cost and consequences could be significant for merchants and consumers in terms of financial cost, brand damage and inconvenience. For merchants in particular, such costs and consequences may far outweigh any 'savings' generated.

3.15 Mastercard makes extensive and ongoing investments in cyber security, not only to protect our technology infrastructure and data but across the payment ecosystem, supporting cardholders, businesses and financial institutions. To maintain the security of our ecosystem, we enable a number of security services when a customer is granted a Mastercard license, ensuring that our customers are taking proactive steps to prevent, identify, detect and respond to fraud and cyber-attacks. We do this using a multi-layered safety and security strategy, supported by integrated security solutions, operating through the complete transaction flow.

3.16 Mastercard provides continuous global network level fraud monitoring, identifying potential catastrophic fraud attacks perpetrated in multiple, global locations. Mastercard pre-emptively alerts issuers about any adverse behaviours that may be occurring from non-domestic locations on BIN ranges potentially exposing the merchant, consumer and card issuer to cyber-attack that will not be detected or prevented by the domestic network. Unlike domestic schemes, Mastercard can actively monitor to help to prevent "man in the middle" attacks by bad actors outside of Australia, helping to minimise fraud against Australian consumers.

Consumer Choice

3.17 In Mastercard's June 2021 submission (**Mastercard's Second Submission**), we noted that unlike other jurisdictions (such as Europe) where similar initiatives are in place, the consumer is not able to influence this routing decision.[10] In Europe, the introduction of the Interchange Fee Regulation (**IFR**) places the decision over the choice of processing infrastructure in the hands of the consumer.[11]

[7] The Initiatives Group (2020), Report on Merchant Acquiring in Australia, p.58
[8] https://help.tyro.com/s/article/Tap-Save-least-cost-routing-FAQs accessed 12 August 2021
[9] See page 3 of the ABA Submission.
[10] For card present transactions, the consumer is only able to exercise a choice over routing at the point of sale by 'dipping' their card. Many consumers are unlikely to be aware of this.
[11] Article 8, Regulation (Eu) 2015/751 of the European Parliament and of the Council of 29 April 2015 on interchange fees for card-based payment transactions

3.18 In assessing any competition benefits associated with LCR, we would encourage the ACCC to assess whether this absence of choice, from a consumer protection perspective, may result in consumers being directed down the route that is less service rich, resulting in consumers having less protection than they initially thought when the transaction was initiated. Mastercard's view is that consumers should be informed and have the ability to choose how their DNDC is being routed.

4. Potential for the mandates in the Proposed Undertaking to have an anti-competitive purpose or effect

4.1 As noted in Mastercard's Second Submission, the use of mandates is not unusual in itself, as many payment schemes have the ability to issue mandates to ensure the effective and secure operation of their networks. The risk with AP+ procuring that the OpCos will develop and make available such mandates is that the mandates may:

(a) benefit each of AP+, BPAY, eftpos and/or NPP more than the organisations required to comply with the mandate, their customers or consumers;

(b) not provide any material benefits to the organisation or their customers that justify the costs to be incurred with such implementation and, given the issues highlighted with legacy systems in the Application, such costs may be substantial;

(c) provide no consumer benefits; and/or

(d) have the potential to effectively foreclose competition from superior or competing products, services or capabilities offered by third parties, or act as a deterrent to alternative competing services being developed and implemented by third parties, including Mastercard.

4.2 As noted in Mastercard's First Submission and Mastercard's Second Submission, the Applicants, who will be influential board members and shareholders in AP+, are effectively the 'gatekeepers' to payments markets in Australia. Mastercard (and Visa) depend on these financial institutions to be able to compete in payments markets. While in their Response, the Applicants deny preferential treatment will be given to eftpos due to shareholder status, they nonetheless state that:

> *"[a] decision by any Applicant not to expend the significant effort required to enable the international scheme offerings is understandable given the proposed functionality is already being provided to the Applicant's end users (eg through NPP)"*[12]

4.3 This shows that if the merger is authorised Mastercard (and Visa) could face more significant hurdles when seeking to expand their offerings and that they will be limited in the extent to which they are able to compete with the Merger Parties across the various low value payment sectors identified as areas of concern by the ACCC.

4.4 As noted in Mastercard's First Submission, a particular concern Mastercard has with the proposed merger is that the ability to compete fairly will become impaired. For example, if a financial institution (including any of the Applicants) is required (via a rule, mandate or otherwise) or otherwise feels compelled (due to the financial commitments they have made) to implement, enable and utilise products, services and/or capabilities of any of BPAY, eftpos or NPP which are inferior to a third party's capability (whether Mastercard's, "Big Tech's" or another entity's):

(a) then competition and innovation between the financial institutions to bring the best payment solutions to the market may be diminished, and it may also prevent those

[12] See page 12 of the Applicants response to submissions from interested third parties dated 19 May 2021 (**Applicants' Response**).

superior third party solutions achieving the necessary network effect, both of which are likely to negatively impact Australian businesses and consumers;

(b) this also has the potential to foreclose competition from superior products, services or capabilities offered by third parties, or act as a deterrent to implement and utilise these superior products, services or capabilities of third parties; and

(c) may also mean, contrary to the claimed benefits of the merger, that those financial institutions are less able to compete with "Big Tech" and their ‘closed loop’ products, services and capabilities given that they have a direct relationship with the financial institutions' customers.

4.5 With respect to each of the undertakings and the mandates attaching to the Prescribed Services set out in Schedule 1 of the Proposed Undertaking, Mastercard would encourage the ACCC to assess the purpose and effect of the service or capability that is subject to a mandate on competition to ensure that these mandates do not raise additional competition concerns, in particular where:

(a) either competing services or capabilities are not mandated, or not currently offered, by Mastercard (Visa and/or other third parties);

(b) the services or capabilities are subject to fees charged by the Merger Parties;

(c) the mandate alone may not have an adverse impact on competition but when considered in the context of the proposed merger and coupled with other rules, mandates, roadmaps of the Merger Parties or otherwise, could have an adverse impact on competition; or

(d) industry wide standards (specifically, an industry-wide Pay with QR Code) are proposed to be developed between the Merger Parties or NPPA without input from other industry participants including Mastercard.

4.6 While Mastercard does not propose to consider the content of the Proposed Undertaking in any detail, we note that:

(a) much of Australia’s existing payments infrastructure operates under standards administered by global standards organisations such as ISO and EMVCo. Payments functionality such as contactless, tokenisation and 3DS referred to in the Proposed Undertaking are already operated in accordance with EMVCo specifications which ensure interoperability both within and outside of Australia, while the Australian Payments Network (**AusPayNet**) has been working on QR code interoperability. Consequently, the undertaking given in 5.6 should either be removed as AusPayNet are seeking to coordinate an industry wide solution, or the undertaking modified to ensure the standards are interoperable, such standards are developed in consultation with other industry participants including Mastercard, and able to be used by all industry participants within Australia including Mastercard and are designed to comply with applicable global specifications, including EMVCo’s QR code specifications.

(b) in assessing the consumer protection perspective recommended in paragraph 3.18 above, the ACCC should not accept any mandate that would not enable consumers to be informed and have the ability to choose how their DNDC transaction is being routed. For example, the description in item 4 on page 13 “Pay for any purchase online - with merchant option for liability shift to issuer” suggests that there may be no disclosure to consumers as to how their transactions are being routed. If this is the case, then it should not be allowed to operate so as to prevent consumers from knowing how their transaction is routed, particularly online where there are additional fraud and security risks.

4.7 It would be a perverse result if the ACCC accepted the Proposed Undertaking, and the effect of these mandates by eftpos was to essentially create a barrier to alternative competing services from Mastercard, or other third parties being developed or implemented, thereby having an adverse impact on competition.

5. Foreclosure risks and access to the NPP infrastructure

5.1 Despite Mastercard and other interested parties highlighting access issues that could present barriers to entry for new participants and/or foreclosure risks, in particular with respect to the NPP, this has not been addressed in the Proposed Undertaking. Mastercard had recommended that [AP+] should provide an undertaking to the ACCC to amongst other things:

(a) give effect to operational separation of NPP from the other [AP+] businesses;

(b) give effect to the implementation of measures to open direct access to the NPP to other payment service providers on non-discriminatory terms, with appropriate dispute resolution mechanisms included to ensure that access disputes can be resolved;

(c) subject to the above, otherwise prevent the NPP from changing the NPP Regulations in a manner that could restrict access to third parties; and

(d) any tender process for the provision of an overlay service on the NPP should be an open and competitive tender process.

5.2 Mastercard refers to 10.1 to 10.8 of Mastercard's First Submission and 5.1 to 5.5 of Mastercard's Second Submission.

5.3 If the ACCC intends to authorise the merger, Mastercard's view is that the ACCC should seek additional undertakings from AP+ to address the foregoing concerns.

5.4 With respect to access, we also note that the Treasury and the ACCC have requested AusPayNet to engage with the industry on standardisation and reusability of existing infrastructure to support and enable action initiation and payment initiation use cases under the Consumer Data Right (CDR) regime. We understand that AusPayNet have highlighted that, as an outcome of CDR action initiation, access should be fair across all participants.