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## **Regulating to reduce Merchant Service Fees**

Restaurant Association of New Zealand submission to the  
Ministry of Business, Innovation and Employment

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## Name and organisation

|                  |                                       |
|------------------|---------------------------------------|
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| Organisation/Iwi | Restaurant Association of New Zealand |

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

The Restaurant Association of New Zealand welcomes the opportunity to make a submission on the *'Regulating to reduce Merchant Service Fees'*.

We are supportive of the Government's appetite to regulate merchant fees as this has been an issue for our members for some time. In a survey of Restaurant Association members, 69% surveyed on this issue submit direct regulation, where the Government regulates, is the preferred option to achieve the objective of reducing merchant service fees.

We submit better clarity and greater certainty of these fees, through an appropriately-weighted regulatory intervention, should prevail.

Bringing transparency to merchant fees will serve our members far better over the long term than allowing a hands-off approach to continue and relying on the banking and payments sector to monitor itself.

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

It is our view the retail payments system has been effectively described and covered in the issues paper.

We agree that there is a two-sided market operating within the retail payment system. However we submit not enough emphasis has been placed on the impact of the 'intermediary' or 'platform' which coordinates the interface between the two sides (being customer and merchant). This interface is where the financial institution operating the card scheme or EFTPOS system can have a major impact on the Merchant side of the equation.

The other gap we have identified is to ensure smaller operators are not overly disadvantaged when new practices are implemented. It is essential that the Government encourages the banking sector to increase the use of plain english and minimize jargon, as the vast majority of SMEs do not live and breathe banking everyday: all operators should have access to clear information so they can make an informed decision about changes, and how changes in this space affect them. Not all SMEs are able to tap into the 'negotiating power' of an Association.

As new technologies emerge, those smaller operators who are working with close margins anyway, will be less able and technically 'qualified' to keep up with the changing nature of business (eg. Digital wallets using Apple Pay).

**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.**

The Restaurant Association of New Zealand appreciates merchant services fees have been an oft-visited issue since 2009 when the Commerce Commission entered into a settlement with 'banks' in relation to alleged anti-competitive conduct in the setting of fees. While this settlement included a range of agreements designed to lower merchant service fees, it has been noted that these fees may be increasing again since the agreement expired in 2013.

Just under 90% of our members believe that the current merchant fee system needs to change. We still experience higher prices in New Zealand than in Australia and the United Kingdom and pay nearly twice as much as Australian retailers pay in merchant fees. On average, we understand it is estimated to be \$13,000 per year more than Australian counterparts.

While there are some positive trends in the move by banks to unbundle their merchant service fees, which on the face of things gives the Merchant more choice, this is unlikely to be taken up by smaller merchants due to the perceived complexity. So while larger organisations, who have the capacity and capability, can benefit from reduced fees, smaller operators remain potentially paying higher rates.

Our members strongly support the Government applying merchant service fee caps to ensure merchants do not face excessive fees; 88% strongly agree with this statement.

As the use of EFTPOS declines, to be replaced by contactless or online payments, operators on a smaller business model will be impacted more heavily by the increased cost of transaction in the 'two-sided' system.

This may have an unfair impact on our members, particularly the smaller operators.

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

The average cardholder believes that their annual fee covers the costs of them using their card and would equally feel that any costs incurred by the merchant to receive payment, should be borne by the merchant as part of the cost of sales.

Merchants especially smaller operators risk losing consumer sales if they look to impose surcharges for different payment types. In addition a merchant is likely to face negative customer response if payment methods are limited and customers in most of our businesses expect operators to accept credit card payments, making it an essential offering.

Some terminals do not distinguish between contactless debit and higher cost credit transactions, and further many point of sale systems do not allow for automatic surcharging which reduces or complicates the merchants ability to recoup those costs.

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

Consumers are reward driven and are largely not across the practice of these reward 'costs' being clawed back or offset through interchange fees at the point of transaction.

Once again, where it is not viable to pass the cost of merchant fees onto the consumer, these may be treated as a cost included in the price of the goods and services.

The higher price for goods and services faced by the consumer may be offset by the benefits received (such as Airpoints), however those who do not pay with credit cards or contactless payment face an increase in price with no corresponding benefit.

The higher prices are incurred by all consumers but only those consumers using a higher cost payment method receive any off-setting benefit.

While banks have moved to offer unbundled and unblended merchant service fees to offer the merchant greater choice, and thereby the ability to control how their fees are structured, the level of complexity and range of fees by payment method will limit uptake, particularly by the smaller operators.

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

We accept that merchant fees are a necessary cost for the service provided. The merchant's ability to recoup these costs, absorb them or include them in the price of goods and services, particularly in the hospitality industry and in light of the monopolistic retail payment system currently in operation, is limited at best.

It is our view that providing clarity on the types of fees, and providing clear and easily accessible options for merchants will make the retail payment system more equitable for all.

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

Based on our experience in the hospitality sector, merchants are limited in their ability to steer customers to low cost payment methods where the consumer receives benefit from using their payment method. Ultimately the customer decides how they want to pay and in some cases, make decisions on where to 'shop' based on payments accepted.

Having said that, historically Diners and American Express cards were widely used, albeit with much higher costs to the Merchant (American Express merchant rates have since reduced to a level comparable to other cards). As a result more and more merchants refused to accept these forms of payments which gradually became accepted by the

consumer who opted for alternative payment methods - this shows that there is some ability to steer customers away from a particular payment method, but it takes time and a 'global' shift to become the norm.

Merchants have been allowed to charge a surcharge when a customer pays by credit card since 2009. It was anticipated that allowing surcharges would provide more transparency on the credit card companies' fees and eventually bring them down. In theory prices should have come down at those businesses that have been imposing a credit card fee as they are able to recoup that business expense. However, that doesn't appear to have been the case.

In addition there have been some concerns that some merchants have set their surcharges at a level that does not reflect their actual cost of accepting credit cards.

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

For the Restaurant Association, this topic has recently come to the forefront through discussions with some of our members advocating for this change and as a result of rate increases across all of the banks.

In 2017, not long after the Government's decision the year prior to monitor the retail payments system and the interchange component of merchant fees since, we wrote to all Members to canvass their views. Even in 2017 there appeared to be a small groundswell advocating for an industry-led initiative around credit card surcharges: just over 40% of our survey respondents indicated that they have considered credit card surcharges for the future. However, many in the sector remained reluctant to introduce credit card surcharges, unless it became more common place.

Another Association survey in 2019 indicated that a small percentage of operators currently apply a credit card surcharge and in 2021 a further survey shows this percentage is growing. Currently around 29% of members apply a credit card surcharge to cover the cost of accepting credit cards. Of those that do, it is still most commonly for large functions such as weddings or large group bookings where it is deemed more fair to put the cost back to the consumer.

Feedback from those that apply a surcharge has been that customers have been overall accepting of the practice. However, as it has not yet been adopted as a 'standard' measure for all credit card transactions, the general opinion is that there is still the potential to offend or lose customers.

Unless surcharging becomes an industry-wide initiative, not all businesses would charge and therefore it could be used as a competitive marketing ploy.

As other industries have begun to impose credit card surcharges, from paying rates online, to booking concert tickets, the consumer discussion around this seems to be more accepting of this extra charge and for that percentage of our operators who have already started applying the surcharge, they report that the consumer response is largely neutral.

Disclosure of the surcharge policy before the purchase is made, to ensure full transparency and that the customer is making an informed purchase will further help mitigate any potential negative impact on the customer.

### **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?**

On the consumer side of the transaction, users of high-costs credit cards are likely to be on higher incomes due to either the issuer rules or self-selection for higher annual fees (eg. Platinum cards) and receive rewards benefits, however the cost the merchants face is passed on to all consumers, including those on low incomes. When the cost of the fees has been built into the cost of goods and services provided, the lower income user pays the higher rate with no offset benefit.

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

Small business merchants will be particularly affected as they are more likely to bear the higher merchant service fees through lack of bargaining power with their acquirers due to the smaller volume of transactions they deal with. An industry survey by the Restaurant Association showed that 68% of respondents had tried to negotiate lower merchant service fees, however results were very mixed, with many indicating they were not successful in securing a different fee.

Due to the complexity of the retail payments system, larger businesses are able to choose from multiple suppliers and payment product types, however a small operator will usually opt into an 'all in one contract' with their bank to simplify connectivity and administration and to avoid having to find their own provider separately.

### **What information or assistance would assist small businesses to obtain better deals?**

Offering (via a website) clearly identified options with comparisons across services offered and prices charged similar to "PriceMe" would assist operators in choosing the service and system that will best suit the size and scale of their operation.

Providing terminals with the ability to apply surcharge on all point of sale systems, when required, with full disclosure to the consumer but with ease of operation for the merchant.

Developing terminals that can be programmed to distinguish between eftpos, debit, credit and contactless payments and apply surcharge where relevant, across all transaction types.

### **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?**

Because of the concentration within a small number of card schemes, effectively the established market schemes have a degree of market power and as banks do not collect fees on EFTPOS transactions from consumers and merchants, the competitive discipline on interchange fees is relatively weak.

The market share of domestic eftpos is declining and there is no incentive for banks to provide contactless functionality on debit cards in store as this product would compete with their scheme debit and credit cards on which they collect merchant fees.

Open banking may create an opportunity for a card-less payment system and may create competitive tension on merchant service fees.

### **What impact is product innovation having on merchant service fees?**

While new payment methods are emerging with new technologies, these are largely being developed to operate using the same 'scheme' rails that existing debit or credit cards currently use, which means the merchant service fee will not only still apply, but may in fact include an additional margin to cover the costs of the digital wallet provider, further perpetuating higher merchant service fees.

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

While we see open banking as having the potential to reshape the competitive landscape and consumer experience, we are cognisant of risk to the consumer, with regards to information sharing. We have no view to provide at this time.

### **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?**

In our view it seems counterintuitive to have governance and oversight of the retail payment system bestowed upon an organisation such as Payments NZ, when the shareholders are the eight banks who derive profits from the debit and credit card schemes.

Implementation of any legislative change should be overseen by an appropriate, third party body. Confidence in the regulatory scheme is the only way, to ensure either the Reserve Bank of New Zealand and/or the Commerce Commission take a dedicated and supervisory role in the retail payment system. Competition and efficiencies of the retail payment system can be implemented through regulatory interventions.

With no regulation or oversight of how fees, particularly the interchange fee, are managed, opportunities for systemic and monopolistic approaches are difficult to mitigate.

## **Do you agree with the objectives for the retail payments system in New Zealand?**

Yes, if the retail payment system's overall objective is to deliver long-term benefits for end-users within NZ and this is achieved through:

- healthy competition between payment providers and payment products
- incentives for beneficial innovation for consumers and merchants
- efficiency in allocating resources through clear price signals, where prices are cost-reflective for the system as a whole

AND

- is fair in its distribution of costs, particularly in its treatment of small business and low income customers.

## **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.**

Ensuring that there is full transparency on the merchant service fees being charged, including the structure of the fee and justification of costs, to allow merchants to understand the level of fees they should be paying and make more informed decisions.

Making the process easier to navigate and understand, where prices are unblended or unbundled, to remove the complexity faced by smaller operators who invariably end up paying a premium for services to retain simplicity.

Providing simple options for enabling membership organisations through collective bargaining to negotiate rates with banks for processing card transactions, which would be available for all of its members:

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

Develop a new governing body that is representative of the stakeholders with vested interest in the management of not only interchange fees but New Zealand's retail system as a whole or consider legislative change to ensure either the Reserve Bank of New Zealand and/or the Commerce Commission take a dedicated and supervisory role in the retail payment system.

Competition and efficiencies of the retail payment system can be implemented through regulatory interventions.



Representatives from those parties involved in the two-sided retail payment system should be invited to participate on any governing body created - SMEs, Hospitality, Trades, Banks, Retailers, Representative Membership Organisations.

**Please provide your views on the impacts of the above classes of options, with supporting evidence of the benefits and costs.**

Codifying rules and practices that would support greater transparency and incentives in the system - this would need to be regulated to ensure that the costs of switching between providers was not prohibitive to the point where it negated any future savings in merchant fees.

Requiring merchants to surcharge for higher cost payment methods or requiring discounts for customers that transact using lower cost payment methods - this would need to be built into the terminal or transactional device to mitigate loss of efficiencies in operation for the merchant. This system potentially open to abuse where merchants still apply a surcharge on lower cost payment methods?

#### **Other comments**

It is essential that New Zealand operates under a sound, secure and supervised retail system to deliver long-term benefits for end-users of retail payments through healthy competition, innovative incentivisation, fair distribution of costs (particularly low income and small business).

A key element of achieving this will be reviewing the regulatory architecture or governance of this system to ensure it remains fit for purpose and is capable of supporting innovation for the benefit of consumers, businesses and the broader economy.

Thankfully, this does not require starting from a blank slate as there has been much achieved in other international markets (Canada, USA, Australia and European Union) who have adopted various interventions and approaches, either by regulation or competitive law action, to ensure a fair system for all.



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