



# **DIGITAL PAYMENTS MARKET: STANDARDIZATION AND COOPETITION**

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Roma 30 settembre 2020



# OUTLINE

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- **Non-bank payment service providers and access to payment systems: security and competition**
- **Interoperability between networks**

# Introduction (1)

- ▶ Traditionally **banks played a prominent role** in the offer of payment services, due to the possibility to bundle payments with other (banking) services such as current account services; the presence of large network externalities and the importance of reputation may have hindered the entry of new players in the market
- ▶ **In the last decades non-bank financial institutions have gained relevant market share in some specific segments**, in particular in the credit card business
- ▶ **Technological innovations** allowed the provision of traditional payment services using innovative means and, in some cases, the offer of new products
- ▶ **Technological innovations have favoured the entrance of new players in the market.** The entry of Big Tech companies, able to collect and manage huge amounts of data about consumer's preferences, could change dramatically the scenario and raise new issues on the effective competition between banks and non-bank networks

## Introduction (2)

- **In Europe policy makers have fostered** innovations in the payment industry:
  - The first Payment Services Directive (PSD 2007) **has set the scene, defining the rights and obligations for a broad spectrum of payment services**, to be offered also by non-bank service providers
  - The new Directive on Payment Services (PSD2 2015) has focused its attention on **security** issues and on the discipline of the **new players entered in the payment domain, the so-called third party service providers**
- Our analysis seeks to understand, in the light of the new regulatory framework, **which are the main areas in which the issues of payment system security and efficiency intersect with those of fostering greater competition for the benefit of cost reduction and availability of easy-to-use and more efficient payment services.**

# Interchange fees regulation: cooperation and competition (1)

- The past case law: the antitrust perspective
  - Multilateral Interchange Fees (MIF) **are horizontal agreements**, therefore subject to scrutiny by the antitrust authorities
  - According to the Commission Decision of 24 July 2002, the MIF in the Visa system amounts to an appreciable restriction of competition within the meaning of article 101.1 of the Treaty on the Functioning of the European Union (TFEU). Nevertheless, **considering that the conditions laid down by Article 101.3 of TFEU are met it could be authorized** (contribution to technical and economic progress; indispensability)

# Interchange fees regulation: cooperation and competition (2)

- ▶ The current regulatory framework: reasons underlying the cap imposed by the legislation (Regulation (EU) 2015/575 on interchange fees for card-based payment transactions (IFR))
- ▶ **Foster the Internal Market competition in card payments and favoring a greater use of electronic payment means, instead of cash**
  - ▶ Indeed, the interchange fees, applied ante regulation, were so high that could act as an entry barrier for new card schemes and, in the past, contributed to the exit of a number of domestic card schemes with relatively low interchange fees
  - ▶ Interchange fees were also found to constitute a floor for merchant fees, below which merchants cannot negotiate, resulting in higher costs to merchant and consumers.

# Interchange fees regulation: cooperation and competition (3)

- ▶ Have the goals, pursued by the European legislator, been achieved after four years from the entry into force of IFR?
  - ▶ Policy papers and the Report by the European Commission (2020) show that, as of the date of entry into force of IFR, the introduction of a ceiling on multilateral interchange fees has **resulted in a substantial reduction in merchant fees** and in a boost in the use of cards. The decline in merchant fees was particularly strong for credit cards.
  - ▶ There is still **no clear evidence that proves the transfer to consumers of the benefit resulting from the reduction of costs by merchants.**

# Non-bank payment service providers and access to payment systems: security and competition (1)

- ▶ In Europe, non-bank payment service providers (PSP) compete with banks in the offer of payment services:
  - ▶ Although PSD2 provisions provides for a non-discriminatory and open access to payment systems **two obstacles limit the creation of a fully competitive market and a level playing field:**
    - ▶ Security reasons allow the payment system operator to deny access to the payment system;
    - ▶ Systems designated under the settlement finality directive are explicitly exempted from the application of the discipline on open access (Recital 40, 50, 51 – art. 35 of the PSD2).



# Non-bank payment service providers and access to payment systems: security and competition (2)

- ▶ According to the PSD2, in all cases in which the regulation cannot provide for direct access to non-bank PSP, 2 conditions should be ensured:
  - ▶ **No discrimination among non-bank PSP;**
  - ▶ **Indirect access by non-bank PSP through bank accounts** (recital 39 and art. 36 of the PSD2).
- ▶ Are these two principle enough to ensure the goals of an effectively competitive market and a level playing field between banks and non-bank payment service providers?

# Non-bank payment service providers and access to payment systems: security and competition (3)

- ▶ **No discrimination among non-banks PSP:**
  - ▶ **When access to non-banks is denied**, effective compliance with the principle of non-discrimination can only be **achieved following interventions by the antitrust authorities**, considering that payment systems are considered essential facilities (exclusionary practices).
  - ▶ **Closed loop systems and three party credit card schemes, are exempted from granting open access** (recital 52 of the PSD2). The goal of this exemption is unclear. The most likely explanation is that the legislator has sought to establish a favorable treatment of newcomers in the payments market. Anyway, if we consider that the exemption will apply to important market players like AMEX and PAYPAL, it is difficult to understand the underlying ratio.

# Non-bank payment service providers and access to payment systems: security and competition (4)

- ▶ **Indirect access by non-banks PSPs through bank accounts**
  - ▶ Currently the **RTGS** (Real Time Gross Settlements) systems **and all systems designated under the settlement finality directive are exempted from granting direct access to non-bank payment service providers.**
  - ▶ In **all Euro countries non-banks PSP are able to access TARGET2, connected with central bank settlement accounts, only indirectly, through the services of a bank**
  - ▶ The reason for this dates back to the origins of central banks and to monetary policy reasons. However, this creates an uneven level playing field between competitors

# Non-bank payment service providers and access to payment systems: security and competition (5)

- ▶ Therefore, in order to enable PSPs to provide payment services, it is **indispensable that they can open and maintain accounts with credit institutions**
- ▶ In 2019 the Bank of England (BoE) decided to extend direct access to RTGS accounts to non-bank payment providers. Indeed the BoE decided to allow non-bank PSPs to open settlement accounts in the BoE RTGS system, subject to appropriate safeguards
- ▶ The very innovative choice of the BoE will allow non-bank PSPs to compete with banks on a more level playing field (they will be less dependent on competitors and will be able to offer a wider range of payment services). **While the benefit in terms of more competition are clear, the impact in terms of financial stability require a deep analysis and empirical evidences.**

# Interoperability between networks (1)

- ▶ The case of **closed-loop payment networks, owned and managed by a Big Tech**, that collects huge and diversified amounts of data about consumer's preferences
  - ▶ **an antitrust issue?** A case of cross-subsidisation? Difficult to prove ...
  - ▶ In any case, there are 2 risks to tackle:
    - ▶ The first risk is that **big-techs can exploit economies of scale related to network effects and have the possibility of bundling different services to gain large market shares, hindering competition**
    - ▶ The second risk is related **to data collection and management**

## Interoperability between networks (2)

- ▶ The case of **closed-loop network owned and managed by a Big Tech**. Is there the need for a regulatory intervention to create a level playing field?
  - ▶ Allowing third parties to access closed loop systems may be an important step
  - ▶ Allowing third parties to access the information collected by Big Techs could be considered, according to the same philosophy which led PSD2 to permit third parties to access information collected by financial intermediaries, with the consent of the user
  - ▶ The access to near field communication (NFC) antennas available on certain mobile platforms (such as phones or tablets) and used for effective contactless payments (the Australian case about Apple Pay and the request of banks to acquire direct access to NFC)

# Interoperability between networks (3)

- ▶ The case of **closed-loop network owned and managed by a Big Tech. Data protection goals explain why a regulatory intervention is important:**
  - ▶ PSD2 established the principle that data are available to the customer who 'generated' them. This allows all players in the payment industry – including Big Techs, if they are willing to enter this market – to collect information on payments, that can be linked with those on purchases and the other they already collect, for example through social media. **In this context, is the usual clause of asking “explicit consent” a suitable measure to protect consumers?**
  - ▶ According to the EU Commission by 2024, the EU should have **an open finance framework in place, in line with the EU Data Strategy, the upcoming Data Act, and Digital Services Act**. This framework will be coordinated with the review of the Payment Services Directive