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Retail Payment System Consultation Team
Commerce Commission
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Draft Decision on interchange fee regulation for Mastercard and Visa networks

Overview

1. Retail NZ is a membership organisation that represents the views and interests of New Zealand's retail sector. We are the peak body representing retailers across Aotearoa, with our membership accounting for nearly 70% of all domestic retail turnover. New Zealand's retail sector comprises approximately 27,000 businesses and employs around 220,000 Kiwis. We have consulted our membership in the preparation of this submission.
2. Retail NZ has long advocated for a more efficient and transparent retail payment system, including lower payment costs for merchants. We strongly supported regulation of the sector under the Retail Payments Act, including the Commerce Commission's role in promoting competition and efficiency within the retail payments sector.
3. We continue to support retailers' legitimate right to apply a surcharge to recover payment costs. To do this accurately they require greater clarity from their acquirers about the fees they pay for different services. Greater simplification and standardisation of fee structures would assist retailers in meeting this objective, as would guidance or regulation addressing how acquirers communicate fees in their customers' bank statements.
4. To gather retailers' input for the consultation, Retail NZ polled its members in February. The focus of our poll was on the value placed on the rewards and benefits of commercial credit cards when weighed against the business benefits of lower interchange fees. Of the respondents, 92% used a credit card for purchasing business items and cited the most valuable credit card benefits as interest free repayment terms and Airpoints dollars. However, 79% of retailers felt that the reduction or removal of these benefits would have low or no impact on them or their business.
5. The responses overwhelmingly indicated that a lower interchange fee was more important than rewards and that lower interchange fees would help profitability for retailers.
6. To complement the poll, Retail NZ held an internal workshop with interested members to gather feedback to inform our submission.

7. As we noted in our submission last year to your consultation on the costs to business and consumers of card payments, merchants and customers have benefited from the technological advancements in payment systems which have provided increased convenience, and speed of transaction, and we continue to see a demand from consumers to embrace technology when making payments. We recognise there is a cost to develop, maintain, and upgrade these technologies but are concerned that the current fees charged for payment services are measurably higher in New Zealand than relevant international benchmarks. We welcome intervention by the Commerce Commission to ensure that fees are set at a reasonable level - sufficient to support the necessary investments and provide a satisfactory return on that investment, without excessive profits being made.
8. Overall, we support the proposal for the Commerce Commission to set lower fee caps for the Interchange component of the designated Mastercard and Visa networks. However, interchange fees account for a little under half the total cost of Merchant Service Fees (MSF) and retailers have legitimate concerns about the cost of other components. A reduction in the interchange fees alone will not address the overall costs that retailers pay via MSF. Retail NZ would like the Commerce Commission to regulate all components of the MSF rather than Interchange fees alone. We are concerned that scheme providers, banks, acquirers and switch businesses will look to increase their fees if the other components of the MSF are left unregulated, even if it is for only a short time until the Commission turns its attention to those other components.
9. We believe that fees should reflect the underlying cost of providing the service, with an appropriate margin to cover capital investment in the system and a contribution to profit which is reasonable. With the information asymmetry, it is unclear whether the current fees can be justified. International benchmarks indicate they are likely to be higher than they need to be. Unfortunately, merchants feel compelled to accept these popular methods of payment even though they do not have sufficient insight into the costs, especially in the current challenging economy. They cannot afford to opt out of these services and reduce customer payment options, as they would potentially lose sales and leave customers dissatisfied.
10. We are pleased that the Commerce Commission has moved to regulate all card scheme providers, and all payment types. As we advised last year, the focus on Mastercard and Visa was too narrow and only partially addressed the issues faced by retailers and the flow-on effects for customers.
11. We note the Commerce Commission is conducting monitoring of some other parts of the retail payments sector and has said it may consider regulating in these other areas in the future. Retail NZ would like to see the Commerce Commission consulting on these issues as a matter of priority.

Retail NZ responses to consultation questions

1. Overall, do you agree with the proposed simplified and lowered interchange fee caps? If not, why not? Please provide reasoning and evidence for the proposed caps you disagree with. (Relevant sections: Chapter 2, Table 2.1)

Retail NZ is pleased to see the proposed reduction in interchange fees. However, we do not believe they go far enough. Our concern is that other components of the merchant service fees will be increased to compensate for the revenue losses incurred by the cap on interchange fees.

Interchange fees were reduced through regulatory means only two years ago. And yet merchant service fees have increased since then.

As one comment in our recent member poll noted:

“When the last legislation was passed to regulate the Interchange fee, almost overnight the Acquiring fee went up!”

We note that the Commission has estimated that capping the interchange fee will mean a reduction of around \$260 million a year which it expects to be passed on to consumers. However, Retail NZ has concerns that the savings will not be passed through. We call on the Commission to ensure that issuers pass on the lower fees to all merchants, not just the larger businesses.

For those customers not on Interchange Plus pricing then the Acquirers (not the Issuers) should be monitored to ensure the interchange fee reductions are passed on to the merchants and appropriate fines issued if the Acquirer is in breach (noting there are now non-bank Acquirers in the New Zealand market).

We continue to encourage the Commerce Commission to consider a cents per transaction approach for debit cards. For debit card transactions fees, larger retailers have been able to negotiate fees on a cents per transaction basis, rather than a percentage, which we expect better reflect providers' underlying cost structures. It is our preference that debit transaction fees are charged on a 'cents per transaction' basis for all merchants rather than a fee as a percentage of transaction value. We have yet to be convinced why a uniform cents per transaction rate should not apply to all merchants. This is a point we would like the Commission to provide more insight on.

2. Overall, do you agree with our reasons for this draft decision, including how this impacts competition and efficiency in the retail payment system for the long-term benefit of merchants and consumers? If not, why not? Please provide reasoning and evidence. (Relevant sections: Chapters 2 and 3)

On the whole, Retail NZ would like to see the Commerce Commission take a more holistic approach to reforming the retail payment system - 'do it once, do it right'. Focusing only on the interchange fee risks distorting the other components of the merchant service fees. While we acknowledge the Commission has said that capping the interchange fee is a first step to

reducing and simplifying payment costs for New Zealand businesses and consumers, we are concerned that a staged process will lead to an unsettling period of continuing change for businesses that already struggle with the complexities of the retail payment system.

Having said that, we support the total MSF fee being less than 1% but we call on the Commerce Commission to ensure the lower interchange fees are passed on to retailers.

As one respondent to our recent poll commented:

“We are a very small business impacted by the high credit card charges. To remain competitive in our retail environment a 1% capped interest rate would be a step in the right direction.”

However, as noted above, our concern is that other components of the merchant service fees will be increased to compensate for the revenue losses incurred by the cap on interchange fees.

Retail NZ members who responded to our survey conclusively indicated that they felt that a lower interchange fee was more important than credit card rewards and that the lower interchange fee would help profitability:

- *“Currently we pay 1.56% service charge on the credit card business transactions that we process. This equates to about \$900 to \$2200 per month depending on sales volume quite a significant business cost. Any reduction would be most welcome in this challenging retail environment.”*
- *“The savings in fees to a business outweigh the benefits in Airpoints or other. A retailer would be better to take the savings and use those instead for travel or the like.”*
- *“You can’t have points to use without paying for them. We believe that it would be much better for the business and customer not to have to pay high fees for making card purchases. Banks should only be charging to cover costs and a small percentage of profit. It always leaves a bad taste in my mouth towards the retail business when I am charged a fee on top of my purchase to ‘cover card fees’.”*

Retail NZ strongly agrees with the Commission that it is important that consumers continue to have the opportunity to utilise payment methods that are not surcharged.

3. Do you agree with our base interchange fee level of 0% for contacted debit and a maximum of 0.20% for contactless debit? If not, why not? Please provide substantive quantitative evidence. (Relevant sections: Chapter 3)

Retail NZ’s preference is for the Commerce Commission to consider a cents/transaction approach for debit cards.

Individual retailers have insufficient knowledge of providers’ costs and/or limited bargaining power to bargain effectively, and all but the largest retailers are price takers. We suspect debit card payment costs are likely to be uniform and we believe a cents per transaction fee would be more appropriate.

As the Commission notes at 3.77, big businesses have the ability to negotiate agreements with the credit card companies that mean the businesses can afford to not surcharge. If the Commission's ultimate objective is for consumers to not pay surcharges, we recommend the Commission examine what high volume large retailers, who do not currently impose surcharges, are paying in merchant service fees.

4. **Do you agree with our view that lower interchange fees are unlikely to have a material impact on fraud protection and are unlikely to materially increase losses to fraud across the retail payment system? If not, why not? Please provide substantive quantitative evidence. (Relevant sections: Chapter 3)**

Retail NZ agrees that lower interchange fees are unlikely to have a material impact on fraud protection. Regardless of what the interchange fees are set at, it is in the issuers' interests to continue to work on fraud protection, to keep their own losses to a minimum and also to protect the reputation and integrity of their payment product.

In retailers' experience, fraud is generally a result of weaknesses in people and processes, rather than the cards themselves. For example, retail staff not following organisational processes in sighting cards or checking signatures.

As a result, the risks and costs of fraud often sit with retailers. If the retailer honours a fraudulent card use, it is the retailer who wears the cost, not the card company.

5. **Do you agree with our view that credit and debit should be treated the same for interchange fees, and our draft decision of no premium on interchange fee rates for in-person credit transactions? If not, why not? Please provide substantive quantitative evidence. (Relevant sections: Chapter 3)**

Retail NZ has no issues with credit and debit cards being given the same treatment. While we are not in a position to provide quantitative evidence, our strong view is that keeping the system simple is much easier for both retailers and consumers.

In addition, we note that merchants should be able to choose what payment types they accept, just as consumers can choose how they want to pay. A merchant should not be forced to accept credit because they accept debit.

6. **Do you agree with our view that commercial transactions do not warrant premium interchange fee rates? If not, why not? Please provide substantive quantitative evidence. (Relevant sections: Chapter 3)**

We agree with this approach. For retailers, a card transaction is the same whether it is a commercial card or not.

- 7. Do you agree with our view that online transactions warrant higher interchange rates than in-person transactions? Do you agree with our draft decision of an interchange fee rate cap of 0.40% for domestic debit and credit online transactions? If not, why not? Please provide substantive quantitative evidence. (Relevant sections: Chapter 3)**

Retail NZ does not agree with this approach. While there may be a higher risk of fraud in online transactions, we do not believe that a differential of 0.2% will create enough revenue for issuers to make any significant investment or effort to deter online fraud. In our view, scheme fees, acquirer costs and margin should be sufficient to cover the risk of fraud.

- 8. Do you agree with our view that foreign-issued cards warrant higher interchange rates than domestically issued cards? Do you agree with our draft decision of an interchange fee rate cap for foreign issued cards used at New Zealand merchants of 0.60% for in-person and 1.15% for online transactions respectively? If not, why not? Please provide substantive quantitative evidence. (Relevant sections: Chapter 3)**

Retail NZ finds it difficult to understand why foreign-issued cards would be treated differently to Visa and Mastercard, unless it can be clearly demonstrated that there are additional costs for foreign-issued card transactions.

For retailers, the approach is the same whether it is a foreign-issued card or not. Charging a higher interchange fee will create added complexity for retailers when our goal is to make the retail payment system simpler and easier to understand.

The foreign exchange rate on foreign issued cards already provides a margin for banks, reducing the need for a high interchange fee rate.

However, retailers have indicated that having a set fee for foreign-issued cards will help lower the overall fees for these transactions, which will make a difference.

- 9. Do you agree with our draft decision to leave interchange fees for transactions using domestic prepaid cards unregulated for now? If not, why not? (Relevant sections: Chapter 3)**

Retail NZ's view is that domestic prepaid cards should be treated the same as debit cards.

Buyers of these cards have paid a premium to purchase them and having paid up front, there would appear to be no additional fees for their use. In addition, issuers benefit from any unspent funds that are left unspent by their expiry date.

- 10. Do you agree with our view that card issuance and currency costs for international payments are unlikely to justify substantive changes to interchange fee rates? If not, why not? Please provide substantive quantitative evidence. (Relevant sections: Chapter 3)**

Retail NZ agrees with the Commerce Commission's views on this point.

11. Do you agree with our proposed new approach for assessing anti-avoidance? If not, why not? (Relevant sections: Chapter 4 and proposed network standard published alongside this paper)

Retail NZ agrees with the need for anti-avoidance measures and encourages the Commission to strongly manage these. In particular, we support the approach for rebates to be reported (4.4).

12. Do you agree with our proposed implementation period (implementation of final pricing standard by 1 November 2025)? If not, why not? (Relevant sections: Chapter 4)

Retail NZ's preference is for the revised interchange fee caps to be in place as soon as possible, and certainly no later than 1 November 2025. Although much work will be needed by all parties to implement the changes, retailers are clear that it must be in place before Christmas.

13. Do you agree that it seems likely that some form of surcharging regulation will be needed? What are your views on the possible options we discuss? Do you see other possible options? If so, which? We welcome feedback on possible options to address excessive surcharging. (Relevant sections: Chapter 5)

Retail NZ supports regulation of surcharging so that all participants in the retail payment system are on a level footing. We continue to be of the view that retailers should be allowed to implement surcharges in order to cover their legitimate costs of accepting credit and debit cards.

That said, we also note that a large number of small retail businesses would like to surcharge their merchant service fees but they do not want to risk giving their customers a bad experience and potentially the loss of sales. For some businesses, surcharging is not an option.

To support any regulation, we strongly recommend improved education efforts by the Commerce Commission. For example, fact sheets need to be short and easy to understand, with relevant examples and/or case studies.

The biggest challenge for retailers, particularly smaller operations, is the complexity of the retail payments system which means that some retailers may be overcharging without realising it. For some time, Retail NZ has been calling for banks to provide accurate advice and information in user friendly formats, to ensure that retailers are making decisions on correct information.

Therefore, any regulations must also extend to the acquirers, to regulate the amounts they charge to retailers for charging surcharges.

As stated earlier in our submission, we would prefer for any surcharging regulation to be implemented at the same time as the cap on interchange fees, as we are concerned that a

staged process will lead to an unsettling period of continuing change for businesses that already struggle with the complexities of the retail payment system.

14. Do you agree with our proposed amendments to the pricing standard? If not, please explain why not and provide an alternative. (Please see the proposed network standard published alongside this paper)

As noted previously Retail NZ would like to see the total merchant service fee regulated, to ensure it does not rise about 1% for domestic credit transactions, and lower for debit transactions.

Conclusion

Thank you for the opportunity to make a submission. Retail NZ is happy to discuss any aspect of this submission further.

No part of this submission should be withheld under the OIA.

Sincerely,



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