2 Background

Scope of the chapter

2.1. In this chapter, we set out the background to the inquiry, and describe the Visa system as it operates in the United Kingdom, and the Access system as it has operated until recently, with comments on the changes to it which are now taking place. We then deal with some issues which arose on debit cards, and with some miscellaneous matters.

The previous inquiry by the Commission

2.2. This is the second occasion on which this Commission have inquired into the supply of credit card services. Their previous report was published in September 1980 (Credit Card Franchise Services: Cmnd 8034).

2.3. The previous inquiry was limited to the services supplied by the credit card companies to traders: that is, to item (i) in the definition of credit card services for this inquiry (see Appendix 1.1). The previous inquiry also covered `charge cards' which, as defined at (c) in the definitions in Appendix 1.1, are excluded from the present reference. In the previous, as in this, inquiry, store cards were excluded (for the definition of these cards see (a) in the definitions in Appendix 1.1). This inquiry therefore covers the supply of credit card services both to cardholders and to traders.

The recommendations and outcome of the previous report

Specific recommendations

2.4. Two specific recommendations were made. The first related to the restriction placed on traders by the suppliers of credit card services, requiring them to charge the same prices for goods or services to customers paying by credit card as to customers paying by other methods (this was referred to in the previous report as the `no discrimination' policy, and is referred to in this report as the No Discrimination rule). The Commission concluded, in the previous inquiry, that that policy operated against the public interest:

> as it has the effects of preventing a trader from competing with other traders by offering different prices to credit card users and other customers, so depriving the customers of an important choice in purchasing goods or services and, in some cases, possibly raising prices generally to all the customers of a trader

(paragraph 11.106(d) on page 185 of Cmnd 8034). The Commission recommended that the suppliers of credit card services to traders should be obliged to abandon the above practice.

2.5. The Government decided against action on the Commission's recommendation, mainly because customers were likely to be inconvenienced or confused, and the display of information on surcharges would impose undue burdens on traders and be difficult to enforce. A copy of the statement made to Parliament on 10 December 1981 is at Appendix 2.1.

2.6. The second recommendation made in the previous report was that discussions between The Joint Credit Card Company Ltd (JCCC) and Barclays Bank Ltd, which might materially affect competition between them, should be abandoned. Matters which had been covered in those discussions included `floor limits' for traders (ie transaction values above which authorisations had to be obtained by traders); rates of interest to be charged to cardholders who took extended credit; the possibility of the introduction of an annual charge to cardholders; the enforcement of the No Discrimination rule on traders; and, occasionally, the merchant service charges (MSCs) charged to, or that might be charged to, particular traders (see paragraphs 11.99 to 11.102 of Cmnd 8034). The two companies subsequently gave assurances to the Director General of Fair Trading (DGFT) that those discussions would cease.

Other concerns expressed by the Commission in their 1980 report

2.7. The Commission were concerned that the profits of at least some of the banks might become excessive and thus might in future be found to operate against the public interest. They calculated profits as percentage returns on capital resources employed (ie the total of shareholders' funds, loan capital, and minority interests employed in credit card services). They concluded that (after deducting branch costs) the level of profitability of the credit card operation of the National Westminster Bank in 1978 was very high, and that, if the pessimistic assumptions put forward by Barclays Bank, in particular, in calculating their profits were discounted, the profits of Barclays Bank and of the Midland Bank in 1978 appeared to be high. The credit card operations of Lloyds Bank and the smaller banks had been slower in becoming profitable. The Commission also compared returns on lending (ie profits, after interest, as a percentage of total funds employed) for the credit card operations with the returns for the banks' total business. They found that the returns for the credit card operations were higher than for the total businesses of the first three banks named above. In the case of the Midland Bank, that conclusion was made after applying the average of all the banks' estimates of branch costs, because the Midland Bank's estimate of those costs was very high (see paragraphs 11.42 to 11.57 and 11.63 to 11.70 in Cmnd 8034).

2.8. The Commission summarised their findings on profitability as follows:

> Profits, high though they have been in some cases in recent years, cannot at present be described as excessive, if only because some allowance must be made for past losses. Nevertheless, if National Westminster Bank were to maintain the present level of profitability of its Access operation, or if the other banks were to reach that level, there would be cause for concern at the profits derived from business in which the banks enjoy a monopoly situation.

2.9. The Commission were also concerned that the structure of the charges levied by the suppliers of credit card services might come to bear hardly on some smaller traders (see paragraphs 11.83 to 11.86 of Cmnd 8034).

2.10. The Commission therefore suggested that the DGFT should keep under review the supply of credit card services, to cardholders as well as to traders, and should consider making a further reference to the Commission of both kinds of services if he judged that the public interest might be prejudiced by developments in those services. While they thought it undesirable to prescribe precisely which factors the DGFT should take into account in his review, the Commission suggested that there would be cause for concern if the credit card market were to continue to grow and so come to represent a much larger proportion of consumer spending, in total or in particular trade sectors, without any sign of new entrants to the market, or if the rates of charge to traders, particularly the high rates, were to show no tendency to decline; or if charges to cardholders were to tend to rise out of line with the general level of interest rates.

The reference of credit card services to the Commission in 1987

2.11. The Office of Fair Trading (OFT) reviewed developments in credit card services in subsequent years, leading to a further reference to the Commission, announced by the DGFT on 27 May 1987. In a press release made on that day, the DGFT said that he had taken into account the following factors among others:

(a) the profitability of banks issuing credit cards appeared to be high and might have reached levels which could be regarded as excessive;

(b) while some additional banks or finance companies had joined the Visa and Access networks in recent years, the monopoly position of the established banks found by the Commission did not appear to have been seriously challenged; and

(c) although lower than interest rates of some other forms of consumer credit, the rates charged to cardholders by Barclaycard and by the Access banks appeared to have remained high in relation to the level of and movements in bank base rates.

The DGFT added that, while he had asked the Commission to focus their attention on credit cards, he expected the Commission to take into account the impact of store cards and charge cards, though those types of card had not been included in the terms of reference for the new inquiry.

2.12. At a press conference held when the inquiry was announced, the DGFT was reported as having listed the seven following subjects which he would expect the Commission to examine in the inquiry:

(1) Were credit card companies making monopoly profits?

(2) Were they charging too high rates of interest, and should interest rates be capped?

(3) Was the period of interest-free credit offered to cardholders fair, since some cardholders were cross-subsidising others?

(4) Was the credit card market sufficiently open to new competition?

(5) Were traders, especially smaller traders, being charged too much?

(6) Should charges to traders continue to be on a percentage basis, or be changed to a flat fee?

(7) Was the No Discrimination rule against the public interest?

THE ARRANGEMENTS FOR THE SUPPLY OF CREDIT CARD SERVICES IN THE UNITED KINGDOM

2.13. While the greater part of the business of United Kingdom credit card operators is domestic, they have considered it necessary to make arrangements for international interchange, so that holders of their cards can use those cards at appropriate outlets overseas, and cardholders from other countries can use their cards in the United Kingdom. The development of the arrangements for international interchange is described in the previous report (Cmnd 8034, Chapter 2, passim). At the beginning of this inquiry, and throughout most of its length, either the Visa or the MasterCard/Eurocard trade marks were used for that purpose, as was the case during the previous inquiry; that is, each bank or other participant used either the one or the other trade mark, but not both (though no restrictions are placed by Visa International Service Association (Visa) or by MasterCard International Incorporated (MCI) or Eurocard International SA (ECI) on United Kingdom suppliers of credit card services using one trade mark from also using the other). A description of the main elements of each system thus operated in recent years is in paragraphs 2.16 to 2.78.

2.14. This division of suppliers of credit card services in the United Kingdom according to their membership of the two principal international payments systems came to an end in the second half of 1988. The reasons given by some banks for the change, and the extent to which suppliers of credit card services have put themselves into a position to offer both Visa and MasterCard/Eurocard services (referred to as `duality'), are described in Chapter 3.

Definitions of credit card services

2.15. As defined in the terms of reference for our inquiry, credit card services consist of:

(a) the undertaking and performance of engagements with suppliers (traders) to pay for goods or services supplied to credit cardholders against the presentation of a credit card, ie to act as a merchant acquirer; and

(b) the undertaking and performance of engagements with the credit cardholder by the person issuing the credit card (or on whose behalf and on whose authority the credit card is issued) to the credit cardholder, ie to act as a card issuer.

The arrangements for the supply of Visa credit card services in the United Kingdom

Membership of Visa

2.16. Visa is a corporation organised under the laws of Delaware, USA, and registered in Great Britain as an overseas company under section 691 of the Companies Act 1985. It is owned and run by its members, who include the United Kingdom Visa banks. Visa itself does not issue any credit or other cards nor does it act as a merchant acquirer.

The United Kingdom Visa banks' arrangements with Visa

2.17. In order to issue cards bearing the Visa logo, including credit cards, the United Kingdom Visa credit card operators have to become members of Visa. Membership entitles them to put the Visa marks on their credit cards, which makes the cards acceptable at all Visa traders in the United Kingdom and world-wide. Membership also obliges them to observe the Visa By Laws and the Operating Regulations.

2.18. In addition membership of Visa gives them access to its international data transmission system providing international interchange (clearance and net settlement data processing) services and authorisation facilities. The Visa system depends on guaranteed payment by the card issuer, either directly by the card issuer to the trader if the card issuer has an agreement with that trader, or via another member with which the trader has an agreement, in which case that member will itself pay the trader and in turn obtain payment from the card issuer. The authorisation service enables card issuers to monitor and control card usage and fraud, while the clearing and settlement data processing services benefit members by allowing them to ascertain their net position vis-à-vis other members and facilitating the settlement of accounts between members. Authorisation and international interchange are fundamental procedures within the Visa system.

2.19. Visa charges fees for the use of its data processing facilities for authorisation and international interchange. Interchange fees are also payable between members for international transactionssee paragraphs 6.67 and 6.68.

2.20. For domestic transactions members are completely free to make their own arrangements. In the United Kingdom, Visa has, on request, provided an authorisation service for all domestic transactions, ie transactions between its United Kingdom members, except for `on us' transactions; that is, transactions generated by credit and other cards for which the card issuer and the merchant acquirer are one and the same. `On us' transactions in the United Kingdom would at present involve the use of credit cards issued by Barclays Bank PLC (Barclays), Lloyds Bank Plc (Lloyds) and TSB Trustcard Ltd (TSB), the latter in respect of its outlets in Northern Ireland only. However, the Visa service is still used in respect of TSB's Northern Ireland traders because Barclays, which carries out the merchant processing on behalf of TSB, does not have direct access to TSB Trustcard card accounts. Visa also provides a clearance service for transactions between all the United Kingdom Visa banks except between TSB and Barclays which have a separate arrangement.

The arrangements with traders

The role of the merchant acquirer in the United Kingdom

2.21. The merchant acquirer (who in the United Kingdom must be a Principal[1] or Associate[2] member of Visa) negotiates agreements (called Merchant Agreements) with traders for them to accept Visa credit and other cards in payment for goods or services. These Agreements set out the conditions on which traders participate in the supply of inter alia Visa credit card services. While some of the terms in Merchant Agreements are required by the Visa rules (see paragraphs 2.22 and 2.65 to 2.70), members are largely left free to agree with traders whatever terms they think fit. Principal members of Visa (and all but two of its present members are Principal members) are eligible to apply to Visa to become merchant acquirers. Visa normally requires Principal members in the United Kingdom to have issued a specific number of Visa cards (not necessarily credit cards) before allowing them to act also as merchant acquirers (see also paragraphs 3.108(c), 6.210 and 6.445). Until recently only two have been merchant acquirers: Barclays (through its Barclaycard credit card operation) throughout the United Kingdom, and TSB Trustcard in Northern Ireland only. TSB also acts as merchant acquirer for two TSB companies which accept Visa credit cards, Swan International Ltd and TSB Trust Company Ltd. Lloyds also began to operate as a Visa merchant acquirer in March 1989.

The processing of Visa credit and other card transactions

2.22. Under the Visa rules, the merchant acquirer must reimburse the trader for the cost of the goods or services provided against the presentation of all Visa credit cards, and then (provided the correct procedures have been followed) obtain reimbursement from the issuer of the credit card presented to the trader, for each transaction. Barclays currently undertakes that process for Visa credit card transactions in the United Kingdom, including those arising from traders which are TSB's outlets (where Barclays acts as processing agent for TSB, which itself reimburses traders), as well as its own outlets throughout the United Kingdom. Since March 1989 Lloyds has also reimbursed those Visa traders for which it is the merchant acquirer.

The merchant service charge

2.23. This is a commercial arrangement between the Visa merchant acquirer and its traders. Each trader receiving the service referred to in paragraph 2.15(a) pays to the merchant acquirer a charge, known as the merchant service charge (MSC) (or `merchant commission' or `discount'), calculated as a percentage of the value of all transactions carried out by means of a Visa credit card (and any cards issued by overseas members of Visa). The trader pays the MSC monthly, in arrears, normally by direct debit.

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[1] A Principal member must issue Visa cards and is eligible to be, but in the United Kingdom need not be, a merchant acquirer.

[2] An Associate member must have a written agreement with the Principal member which sponsored it for membership to supply credit (and other) card services. There are two Associate members in the United Kingdom: the Airdrie Savings Bank, sponsored by the Bank of Scotland, and Mercantile Credit Company Ltd, sponsored by, and a subsidiary of, Barclays.

Banking of Visa sales vouchers

2.24. The Merchant Agreement also specifies what the trader must do to obtain reimbursement. Provided that the correct procedures have been observed, Visa sales vouchers can be `banked' by a trader at any branch of any United Kingdom Visa bank nominated or agreed by the merchant acquirer from which they are (if necessary) transmitted through the bank giro to the branch of the bank holding his account. (This need not be a United Kingdom Visa bank.) If the trader pays his Visa vouchers into an account with a Visa bank at the branch holding his account, he receives immediate cleared funds, ie the vouchers are equivalent to cash. Traders who are customers of Girobank plc (Girobank) and have agreements with Barclays and TSB for Visa transactions and with the JCCC for Access/MasterCard/Eurocard transactions can now bank their vouchers at post offices. Girobank is seeking the same arrangements with new or prospective merchant acquirers as it now has with Barclays and the JCCC.

The arrangements between Barclays as merchant acquirer and the other United Kingdom Visa banks

2.25. Barclays has negotiated agreements, called Domestic Interchange Agreements, to deal with the authorisation and interchange of Visa card transactions in the United Kingdom, as between Barclays and each of the other United Kingdom Visa credit card operators. Under these Agreements Barclays passes on to the other United Kingdom Visa member the income it has received, by way of the MSCs paid by traders, in respect of all transactions involving the Visa credit card issued by that member (in practice, this is done by applying an average percentage MSC to the transaction turnover). Before doing so, Barclays deducts charges negotiated separately with each United Kingdom Visa member, to recover its own costs, in particular, for servicing trade outlets, and processing transactions and a margin of profit.

2.26. In February 1989 Barclays gave notice of termination of its Domestic Interchange Agreements with all other United Kingdom Visa members, with effect from 15 May 1989, and proposed that the interchange fee should be set at 1 per cent of net retail sales, as provided in Visa's Operating Regulations if its members in any country cannot agree on the level of the fee. Barclays gave us several reasons for this decision. The decline in MSCs could lead to other card issuers receiving less than 1 per cent which might cause them to give notice of termination of their Agreements; Barclays preferred to make the change at a time which fitted its own business plans. The entry of other Visa merchant acquirers also meant that Barclays needed to review the Agreements to guard against detriment to its own interests. Visa's Operating Regulations offer a uniform system which, with the large number of United Kingdom Visa card issuers and, soon, other United Kingdom Visa merchant acquirers, will be much simpler to administer. The immediate effect of the change would be to give Barclays the greater part of the MSC income, because the average rate is at present greater than 2 per cent. Barclays pointed out that a further reduction in the rate could lead to the merchant acquirer's share becoming insufficient, and its operation uneconomic.

2.27. At the time of completion of our report, discussions between Barclays and the other United Kingdom Visa members on the level of domestic interchange fees and on arrangements for other matters dealt with under the present Domestic Interchange Agreements were continuing and no final agreement had been reached though in some cases Barclays had agreed to continue, for a trial period, authorisation and processing services for cash advances made at the relevant United Kingdom Visa members' branches. One possibility is that Visa may be approached to arbitrate on the level of interchange fee.

Restrictions placed by Barclays, in its Domestic Interchange Agreements, on the freedom of some other United Kingdom Visa card issuers to promote their credit cards in competition with Barclaycard

2.28. In its Domestic Interchange Agreements entered into with three other Visa card issuers Barclays had placed certain restrictions on the extent to which those card issuers could promote existing, or launch new, Visa credit cards in competition with its own credit card (Barclaycard).

Barclays told us that it had not sought to include similar clauses in Domestic Interchange Agreements with other Visa card issuers, that the relevant clauses had not been enforced, and that all the Domestic Interchange Agreements were being terminated or renegotiated (see paragraphs 2.26 and 2.27). These clauses would not be included in any new agreements with any Visa card issuers.

Arrangements with Visa cardholders

2.29. The services supplied to credit cardholders (see paragraph 2.15(b)) and the arrangements for supplying those services are matters for decision entirely between the Visa card issuer and the cardholder, except as prescribed by the requirements of the Consumer Credit Act 1974 and Regulations made under that Act. None of Visa's By Laws or Operating Regulations affect those services or arrangements (except that the cards themselves must conform with Visa's requirements as regards trade marks and other specifications ensuring uniformity and universal usage). Therefore, United Kingdom Visa credit card issuers are in a position to compete with each other, as well as with other suppliers of credit and other card services, in supplying these services.

2.30. In the past, including at the time of the previous inquiry, Barclays issued Visa credit cards as agents for some other banks (whose names appeared on the cards) and undertook tasks such as authorisation, the processing of transactions, and despatch of monthly accounts to cardholders (on reimbursement by the other banks). Barclays told us that it no longer performs that service for any other Visa credit card issuers. Some Visa card issuers (for example TSB, the Bank of Scotland (BoS), Co-operative Bank plc (Co-op) and Girobank) have set up their own processing facilities, so that they now undertake all their own processing so far as services to cardholders are concerned, as well as being able to undertake such work for other parties.

The terms and conditions of use applying to Visa credit cardholders

2.31. The conditions of use of the Visa credit card are drawn to the attention of the potential cardholder as part of the application form which has to be completed before a card can be issued, and are part of the agreement between the card issuer and the cardholder. Some of the main conditions of use or obligations falling on the credit cardholder are set out below; they are similar (and often identical in wording) for nearly all the United Kingdom Visa members which issue credit cards:

Credit limit

(a) The card issuer determines and notifies to the cardholder the credit limit, ie the maximum debit balance permitted on the card account.

Monthly account

(b) The card issuer normally sends a monthly statement to the principal cardholder who is required to pay, within 25 days following the date of the statement, not less than 5 per cent of the amount shown in the statement to be due to the card issuer, or £5 (whichever is the greater), or the full amount due if less than £5. The principal cardholder is also required to pay immediately any outstanding excess over the credit limit, any arrears of previous payments and the amount of any card transaction made in breach of the terms of the agreement.

Interest and other charges

(c) Interest is charged on a daily basis at a stated rate per month on the balance outstanding on the monthly statement date from that date until any repayments are credited to the card account and thereafter on the reduced balance up to and including the next statement date when the interest will be debited to the card account.

(d) If, however, the whole of the balance (whether on account of purchases, cash advances or otherwise) which is outstanding on the monthly statement date is repaid by the close of business on the 25th day following that date, no interest will be charged on that balance.

(e) A handling charge of 1.5 per cent on the amount of any cash advance is immediately debited to the card account for each advance.

(f) No charge is made for the issue or reissue of any Visa credit card.

The arrangements for the supply of Access credit card services before dual licensing existed in the United Kingdom

2.32. Paragraphs 2.34 to 2.62 describe the Access credit card scheme as it operated up to the early part of 1989, and as it still operates in respect of most Access trader and cardholder transactions. From March 1989 Lloyds and later Midland Bank plc (Midland), National Westminster Bank PLC (NatWest) and The Royal Bank of Scotland Group plc (RBS) began to act as a merchant acquirers for Access/MasterCard/Eurocard transactions. As a result the JCCC has ceased to be the only merchant acquirer on behalf of the Access banks; and Midland and later NatWest began to issue Visa credit cards. These developments, and the changes in the role and future of the JCCC, are described in paragraphs 3.104 to 3.110.

2.33. The suppliers of Access credit card services use the MasterCard/Eurocard trade marks, which are the only significant alternative to Visa for international interchange when the issuing of cards and the acquisition of merchants are undertaken by different bodies. While the Access credit card services are in many respects similar to those provided by United Kingdom Visa members, as already described, there are important differences, in particular arising from the position of the JCCC within the Access scheme.

The arrangements of the Access group

2.34. Access credit cards, using the MasterCard and Eurocard as well as the Access trade marks, are issued in the United Kingdom by the following banks (henceforth referred to as `the Access banks'): Lloyds, Midland, NatWest, RBS, the Bank of Ireland, Clydesdale Bank, and Northern Bank. The Clydesdale and Northern Banks, previously owned by Midland, are now owned by National Australia Finance Ltd (NAF). Northern Bank began issuing Access credit cards in its own right in November 1988; Clydesdale Bank had issued Access credit cards through Midland until October 1988, when it began issuing Access cards in its own right.

2.35. The JCCC is a private company, set up in 1971 by the first three of the banks named in the preceding paragraph, which, together with RBS, own all the JCCC's shares. Each of the four banks nominates a non-executive director of the JCCC, one of whom acts as Chairman of the Board, which has six members. The four banks together therefore control the JCCC. The other Access banks are not shareholders, but have made other arrangements to enable them to participate in the Access group credit card scheme.

2.36. The JCCC performs three main functions in the Access credit card scheme:

(a) It is the proprietor of the Access trade marks, and the principal United Kingdom licensee of the MasterCard and Eurocard trade marks which give the Access credit card its international acceptability.

(b) It acts as merchant acquirer.

(c) It carries out processing and other services related to traders and cardholders on behalf of the Access banks.

2.37. Each individual Access bank supplies the remaining parts of the Access credit card services; in particular each Access bank decides whether to issue a credit card to a person, the terms and conditions to be offered to its cardholders, including the determination of the interest rate, provides credit, monitors the accounts of cardholders and deals with overdue payments and bad debts, and complaints from cardholders.

2.38. The roles of the JCCC and the individual Access banks are described in more detail in the following paragraphs.

The roles of JCCC

(a) Trade marks

The Access trade marks

2.39. As proprietor of the Access trade marks the JCCC has entered into agreements with each of the Access banks, giving each bank a non-exclusive right to use the marks `in such manner as [the JCCC] shall from time to time direct'.

The MasterCard trade marks

2.40. The owner of the MasterCard trade marks is MCI, a membership corporation organised under the laws of the State of Delaware, USA. These trade marks enable MasterCard cards bearing the Access mark to be used at merchants around the world where the MasterCard card is accepted for payment. The JCCC is a Principal (Association) member of MCI; it has a non- assignable licence to use the MasterCard trade marks in the United Kingdom, in accordance with MCI's Bylaws and Rules. The participating Access banks were previously affiliate members of MCI, having agreements with MCI whereby each confirmed that the JCCC acted as agent for all of them, and each undertook to use the trade marks only in a manner agreed between MCI and the JCCC. The banks are now also Principal members of MCI.

The Eurocard trade marks

2.41. These trade marks, which appear on the back of the Access MasterCard card, are owned by ECI, a company which has organised an international credit card system, with a head office in Brussels. The JCCC is a licensee of the Eurocard trade marks in the United Kingdom, and so too are the Access banks which had previously been authorised by the JCCC to use those marks. As described in the following paragraph, the licensing and use of the MasterCard and Eurocard trade marks is, in Europe, a joint operation.

The arrangements between MCI and ECI

2.42. MCI has delegated to the Board of ECI initial licensing authority in relation to MasterCard trade marks in Europe.[1] ECI suggests that an applicant for a MasterCard licence should apply simultaneously for a Eurocard licence. If the applicant agrees to take both licences it is required to combine the trade marks with the Eurocard and MasterCard logos. Outside Europe, Eurocard has no licensing power with respect to the MasterCard marks and the MasterCard marks generally appear alone rather than in conjunction with the Eurocard or Access marks. In Europe, the Eurocard marks are used in conjunction with the MasterCard marks. The European merchant network was created largely by Eurocard licensees. All Eurocard cards bear the MasterCard logo and traders accepting such cards must also accept MasterCard cards which do not bear the Eurocard logo. Access cards carry the MasterCard logo on the front and include the Eurocard logo on the back of the card.

[1] A list of the countries to which the arrangement applies is at Appendix 2.2.

(b) The JCCC as merchant acquirer for the Access group

2.43. The JCCC used to be the sole merchant acquirer in relation to Access transactions, but as explained above (see paragraph 2.32) this is no longer the case. Some of the functions performed by the JCCC and described in the following paragraphs are now also being performed by Access banks.

2.44. The JCCC is responsible for the recruitment of traders and maintenance of the Access trader network, negotiating the agreements by which they undertake to accept Access credit cards, establishing floor limits above which authorisation of a transaction has to be sought, training traders' staff and dealing with any queries or problems traders may have. The JCCC reimburses the Access banks for payments made to traders on banking of their vouchers or magnetic tapes, and is in turn reimbursed by the Access banks which issue the cards on which the transactions were effected.

2.45. Provided that the correct procedures have been observed Access sales vouchers can be `banked' by a trader at any branch of any Access bank. If that is not the branch which holds the trader's account, that branch will arrange for the trader's account to be credited through the bank giro. If the trader pays his Access vouchers into the Access bank branch holding his account, he receives immediate cleared funds, ie the vouchers are equivalent to cash. Traders who are customers of Girobank and have agreements with Barclays and TSB for Visa transactions and with the JCCC for Access/MasterCard/Eurocard transactions can now bank their vouchers at post offices. Girobank is seeking the same arrangements with new or prospective merchant acquirers as it now has with Barclays and the JCCC.

2.46. The JCCC negotiates with traders the MSCs which they are required to pay in return for services related to Access credit cards under the Access/MasterCard/Eurocard trade marks. The MSC is calculated as a percentage of the value of each transaction carried out by means of Access credit cards or MasterCard/Eurocard credit cards which the trader has agreed with the JCCC to accept. The charge is normally paid by direct debit in response to the monthly account sent to the trader by the JCCC.

2.47. The JCCC provides the authorisation service for dealing with transactions exceeding floor limits (for cash advances made by the banks other than through Automated Teller Machines (ATMs) as well as transactions by traders). It also deals with queries from a trader who is suspicious about a cardholder, or about a card which is on the lost or stolen lists. Some authorisation requests may also involve the Access departments of the individual Access banks. The costs of telephone calls made for authorisation purposes are refunded to traders.

2.48. The JCCC also settles all international transactions, involving use of Access credit cards abroad, or use in the United Kingdom of cards of associated card schemes issued abroad, including all MasterCard and Eurocard cards.

2.49. The JCCC is responsible for fraud control so far as traders are concerned. This includes attempts to recover lost or stolen cards (including circulation of lists of such cards); testing of the validity of the levels of floor limits at selected traders, and efforts to deal with exceptionally high levels of fraud, at individual traders or in trade sectors or in geographical areas. (Each Access bank bears the actual losses from bad debts or fraud arising from the cards which it has issued, and the expense of circulating its own `hot card' notices.)

2.50. The JCCC is also responsible for the general promotion of the Access brand, including a central advertising programme. This role also covers general promotion held in co-operation with selected trade outlets. The JCCC also provides traders with marketing information derived from its processing operations.

(c) The JCCC's involvement in the supply of services to cardholders

2.51. The JCCC (acting as an agent for each Access card-issuing bank, and at cost to each bank) carries out the following functions:

(a) it maintains a network of trader outlets at which Access cardholders can use their credit cards;

(b) it maintains the master computer file of all Access credit cardholders (from data supplied by each Access bank);

(c) it produces and despatches new and replacement cards, on instructions from the Access banks (some of which also issue some cards themselves);

(d) on instructions from the Access banks it prepares and despatches monthly statements to cardholders, and records their payments: the service includes sending marketing leaflets etc with the statements, for the individual Access banks if they wish to use it;

(e) it processes refunds to cardholders where transactions with traders are involved;

(f) it is involved, with the Access banks, in dealing with claims relating to connected lender liability under section 75 of the Consumer Credit Act 1974 (if the JCCC is unable to resolve a claim to the satisfaction of the cardholder, the latter can pursue the matter further with the card-issuing bank);

(g) it provides information when required to assist the Access banks in dealing with complaints from cardholders, including those involving traders;

(h) in order to combat fraud, it checks on all applications for new Access credit cards to see whether the same person is making more than one application (some of the Access banks can do this in respect of their own cardholders); and

(i) it prepares a variety of data and statistical reports on cardholders' accounts for each Access bank's separate use.

The role of the individual Access bank

2.52. Each bank's actions as regards the Access scheme relate primarily to the provision of services to its own cardholders; in this respect, the bank is acting primarily in the interests of its customers and itself, and is or may be competing against the other Access banks, eg in recruiting cardholders.

2.53. Each bank decides to whom its Access credit cards shall be provided; the terms and conditions to be offered to cardholders including such matters as the rate of interest to be charged for credit supplied; and the rules for payment of monthly accounts. The agreement between the Access banks on matters such as those, which was in force during the previous inquiry, was terminated in 1981. Each bank has its own arrangements for monitoring its cardholders' accounts, reviewing their credit limits, dealing with the exceeding of credit limits, overdue payments, and bad debts, withdrawing cards and so on. Each bank deals with complaints from its cardholders (with the JCCC's assistance if required) and makes arrangements for them to report lost or stolen cards. Each bank takes steps to reduce loss or fraud, eg by checking on dormant accounts before replacement cards are sent out; `recapturing' in ATMs cards that have been withdrawn from cardholders; imposing floor limits on its branches for cash withdrawals, and applying the necessary precautions in its branches for lost or stolen cards.

2.54. Each Access bank can promote and advertise its own credit card in any way in which it wishes to do so. But partly because of the JCCC's central role in promotion (see paragraph 2.50) rules have been agreed between the JCCC and the Access banks governing in particular the promotion of the Access brand and the individual bank cards. These are set out in a document called `Access Principles', a copy of which is at Appendix 2.3.

The financial arrangements of the Access scheme

2.55. The costs which each individual Access bank incurs in carrying out its own functions (see paragraphs 2.52 to 2.54) and the income it obtains directly, which is mainly by way of interest payments from its cardholders, are for its own account.

2.56. All the Access bankswhether shareholders in the JCCC or notjointly participate in the financial arrangements with the JCCC. As regards capital costs, the shareholder banks contribute in the form of loan capital in proportion to their shareholdings. Non-shareholder banks pay an annual Franchise Fee, equal to 10 per cent of a proportion of the net book value of the JCCC's fixed assets, the proportion being that which the number of that bank's cardholders bears to the total number of cardholders. As regards the JCCC's other costs incurred on behalf of all participants, any surplus of the JCCC's income over those costs is distributed among the participant banks (whether shareholders of the JCCC or not) in accordance with an agreement, called the Formula Agreement, the latest version of which dates from 30 October 1987. The principle underlying the agreement is that each bank bears its share of the JCCC's costs, and receives its share of the JCCC's income (from the MSCs), in proportion to the amount of business generated by its cardholders. So far as income is concerned, this is allocated directly to the bank which issued the card generating it (ie income follows the card); in the case of costs, the proportions are those represented by the number of vouchers arising from traders' transactions generated by each bank's cardholders compared with the total number of such transactions processed by the JCCC's computers and the number of cash advances made to each bank's cardholders compared with the total number of cash advances processed by the JCCC's computers. This arrangement gives each Access bank an incentive to increase the numbers of its cardholders and the amount of business generated on its cards.

2.57. The result of applying this formula has been, taking the years 1984 to 1988 together, that just under 51 per cent of the JCCC's total income has been passed on to the participating banks as a whole; each bank's share (ie the surplus received, as a proportion of the amount of the JCCC's income generated by that bank's cardholders' activities) has also been close to 50 per cent of its share of income during that period. The surpluses were passed on after the JCCC had recovered all its costs in providing services common to all participants; those services included a considerable amount of processing and other activities related to cardholders (see paragraph 2.51), in addition to its function as merchant acquirer, although the JCCC's costs exclude many of the costs associated with providing services to traders such as the costs of bad debts, and of credit, which are incurred by the banks. The amounts involved were:

	1984 to 1988 *£m*
1. Total income (MSCs)	661.7
2. Total surplus to participating banks	335.2
3. Of which, the individual banks received:	
(a) Lloyds	87.3
(b) Midland	95.6
(c) NatWest	126.0
(d) RBS	21.1
(e) Bank of Ireland	5.2

2.58. The surpluses passed to the Access banks have represented around 1.1 per cent of the total annual value of Access transactions (including cash advances) during the period.

2.59. The JCCC told us that the arrangements under the Formula Agreement are being phased out and the JCCC is moving to being remunerated on a tariff basis for the services which it provides, whether for the existing banks or for new customers.

2.60. The MasterCard and Eurocard systems determine the interchange fees to be paid for international transactions. The JCCC currently pays 1 per cent of the net value of the transaction with a United Kingdom trader to the foreign card issuer concerned; the converse also applies. The international interchange fee covers costs that are related to the issuing of cards, including the cost of credit advanced, of fraud and counterfeiting, processing costs and the increased risk arising in international transactions. Up to now, domestic interchange fees have not been paid between the members of the Access scheme in the United Kingdom; instead, the arrangements described in paragraphs 2.56 to 2.58 have applied. But that situation will change as a result of the developments in merchant acquiring mentioned in paragraph 3.108.

Arrangements with Access cardholders

2.61. The services supplied to credit cardholders and the arrangements for supplying those services are matters for decision entirely between the Access card-issuing banks and the cardholder. None of MCI's or ECI's rules affect those services or arrangements (except that the cards themselves must conform to their requirements as regards trade marks). Therefore, Access card issuers are in a position to compete with each other, as well as with other suppliers of credit card services, in these matters.

The terms and conditions of use applying to cardholders

2.62. The conditions of use of the Access credit card are drawn to the attention of the potential cardholder as part of the application form which has to be completed before a card can be issued, and are part of the agreement between the card issuer and the cardholder. Some of the main conditions of use or obligations falling on the cardholder are set out below; they are similar for all the Access banks:

Credit limit

(a) Each bank determines and notifies to the cardholder the credit limit, ie the maximum debit balance permitted on the card account.

Monthly account

(b) The JCCC on behalf of the Access banks normally sends a monthly statement to the principal cardholder who is required to pay, within 25 days following the date of the statement, not less than 5 per cent of the amount shown in the statement to be due to the bank or £5 (whichever is the greater) or the full amount due if less than £5. The principal cardholder is also required to pay immediately any outstanding excess over the credit limit, any arrears of previous payments and the amount of any card transaction made in breach of the terms of the agreement.

Interest and other charges

(c) Each bank charges interest on a daily basis at a stated monthly rate.

(d) No interest is charged on the amount of purchases (but not cash advancessee (e) below) repaid by the cardholder and credited to the account within 25 days of the date of the statement of account on which those purchases first appeared. The daily balance of any such amounts outstanding at the end of the 25-day period is charged interest from that statement date until full repayment is credited to their account.

(e) Cash advances bear interest on a daily basis from the date the advance is made until it is repaid.

(f) No charge is made for the issue or reissue of any Access credit card.

2.63. As noted in paragraph 2.32, the operation of the Access scheme began to change in the early part of 1989. In particular, the role of the JCCC is changing fundamentally; it is moving rapidly towards becoming a supplier of processing and other services. The four Access shareholder banks are all now Principal licensees of MasterCard/Eurocard, and are operating as merchant acquirers for Access/MasterCard/Eurocard transactions. Many of the JCCC's staff involved in merchant acquisition have been recruited by one or other of the Access banks. The role of merchant acquisition is ceasing to be one of the JCCC's main functions. The ownership and management of the Access trade marks is being transferred to a separate legal entity. The JCCC's Board has agreed new objectives for the processing company consisting of acquisition processing and issuer processing, for both Access/MasterCard/Eurocard and for Visa transactions, for Access members and other organisations; and acquisition and issuer processing for other card schemes on behalf of third parties. By about the middle of 1990 the JCCC is likely to have fully completed the transition from its traditional role to that of a provider of services to financial institutions on an arm's length basis.

Comparison of the terms and conditions applying to Visa and to Access cardholders

2.64. A comparison of paragraph 2.31 with paragraph 2.62 shows that, in some respects, the Visa and Access terms and conditions are the same, in particular as regards payment terms (b) in each paragraph. The charging of interest, when due, for purchases, and the charges made for cash advances are different, but only as between the two systems; within each system, card issuers generally follow the same practices or arrangements.

Some Visa or MasterCard rules applying to traders

2.65. Issues relating to two rules applied by Visa and by MCI/ECI and affecting traders have arisen in this inquiry. The rules are, first, the Honour All Cards rule, which requires traders to accept all Visa or all MasterCard/Eurocard cards, as the case may be; and, second, the rule (broadly) requiring traders to offer goods and services to credit card customers on the same terms, including price, as to all other customers (to which we refer, throughout this report, as the No Discrimination rule). The position on these rules is set out in the following paragraphs.

Honour All Cards rule

2.66. The essence of Visa's Honour All Cards rule, in its Operating Regulations, is as follows:

> 6.03 *Honor All Cards*
> The Traditional Visa Merchant shall promptly honor all valid Classic Visa Cards and Premier Visa Cards when properly presented as payment from Cardholders for Transactions
> …

MasterCard's rule (which applies also to Eurocard) is set out in paragraph 2.71 since it is combined with its No Discrimination rule.

No Discrimination rule

The Visa rule

2.67. Visa's Operating Regulations require traders who accept Visa credit (and other) cards not to impose any surcharge on transactions when a Visa credit card is used. The relevant part of the Regulations reads as follows:

> 6.03B The Merchant shall not impose any surcharge on transactions unless local law or regulation specifically requires that the Merchant be permitted to impose such a surcharge on credit card transactions.

2.68. The Commission understand, from oral evidence given to them by Visa, that in its view the rule also covers discrimination against holders of Visa credit cards by means of discounts offered by traders to customers who use forms of payment other than such cards.

Barclays' and TSB's agreements with traders in the United Kingdom

2.69. In their agreements with traders, Barclays and TSB, in order to comply with Visa's rule on this matter, have included the following provisions:

Barclays

The Merchant will: `… Honour all Cards presented and may also accept mail or telephone orders against Cards in consideration of the supply of goods, services or other facilities on the same terms (including price) as they are supplied for cash;'

TSB

`Acceptance of cards
Goods and services shall be offered by a Merchant to customers paying with a card on terms identical to those which would be offered to customers paying by cash.'

2.70. Although the Visa rule refers only to surcharging, Barclays' and TSB's rules cover any departure from the cash price, and therefore also prevent discounts for cash or cheque payments being offered. Barclays explained that its rule was drafted to reflect what it understood Visa's policy to be. TSB explained that it had referred to cash terms in its current agreement, to remove the ambiguity in its previous agreement, which had referred to `normal' prices.

The MasterCard/Eurocard rule

The Honour All Cards and No Discrimination rules

2.71. Subsection 9.04 b(1) of MasterCard's Rules (which apply also to Eurocard) states:

(1) Honor MasterCard Cards. The merchant shall honor without discrimination all valid MasterCard cards when properly presented as payment from customers for transactions and shall maintain a policy that shall not discriminate among customers seeking to make purchases through use of a MasterCard card ….

2.72. Subsection 9.14 b(14) of the Rules states:

(14) Charges to Cardholders. The merchant shall not require any MasterCard cardholder to pay any part of any merchant discount, whether through any increase in price or otherwise, or to pay any contemporaneous finance charge in connection with the transaction in which a MasterCard card is used. `Merchant discount', as used in this Subsection, means any charge made to the merchant for the acquisition of sales slips negotiated by the merchant and the member or affiliate with which the merchant has a merchant agreement. The prohibitions of this Subsection (14) shall not be construed as prohibiting discounts for payments in cash.

2.73. The JCCC includes the following clause in its Retailer Agreements:

(4) The Retailer agrees to honour all valid and current Access Cards (which term shall include any other credit cards which the Company shall notify the Retailer are to be accepted by the Retailer) presented by the proper holders thereof (hereinafter called `Cardholders') by supplying to Cardholders, without imposing any minimum financial limit upon any transaction, such of the full range of the goods or services (except as may be otherwise agreed in writing between the Company and the Retailer) offered by the Retailer to customers of the Retailer as any Cardholder may request, at the Retailer's normal price for such goods or services ….

2.74. The above clause does not permit Access traders to offer discounts for cash, though the MasterCard rule does not prohibit such discounts.

Visa and MasterCard's rules on card issuing and merchant acquisition by their members

Visa

2.75. Virtually all United Kingdom Visa members who at present issue cards or acquire merchants are Principal members.

2.76. Visa's rules on the obligations of a Principal member, in its By Laws, include the following:

> Section 2.05. Principal Membership. In accordance with the International Operating Regulations, a Principal shall either directly or by contract with other members:
>
> *(a)* Actively develop, maintain and service direct contractual relationships with holders of bank cards bearing either or both of the marks, VISA and Blue, White and Gold Bands Design and/or marks associated with an Electron card program adopted by the appropriate Region, and with merchants which agree to honor such bank cards and Travel Vouchers.

MasterCard/Eurocard

2.77. The MasterCard rules lay down that a financial institution, organisation or corporation that participates in any card activities or that uses any of the MasterCard or Eurocard card trade marks must become a card member.

Specific obligations of card membership

2.78. The MasterCard rules require that, within one year of becoming a member and at all times thereafter, each member must have issued and outstanding a reasonable number of MasterCard/Eurocard cards. That number is set in relation to the population of the metropolitan area in which the member has its principal office as follows:

Approximate population	*Minimum number of MasterCard cards to be issued*
Under 50,000	500
50,000 to 100,000	1,000
100,000 to 250,000	2,500
250,000 to 500,000	5,000
500,000 to 750,000	7,500
Over 750,000	10,000

(See also paragraph 6.482.)

DEBIT CARDS

2.79. Debit cards are plastic payment cards which can be used to purchase goods or services from traders. They do not directly provide cardholders with credit, and are themselves therefore not within our terms of reference. Barclays introduced the first debit card in the United Kingdom, the Connect Visa card (Connect), in April 1987. This was followed by the Lloyds Visa payment card in mid-1988, and, a little later, by the Switch debit cards, issued by Midland, NatWest and RBS.

2.80. Two issues were raised with the Commission in relation to Connect and other Visa debit cards. First, some trade associations and individual traders complained about the MSCs which Barclays had sought to negotiate for Connect (see paragraphs 2.82 to 2.84). Second, J Sainsbury plc (Sainsbury's) complained that Barclays would not enter into an agreement with it to accept Visa debit cards unless it also accepted Visa credit and all other cards. In both cases, therefore, the issues were related to the supply of credit card services.

2.81. Both cases also involved the application of the Visa Honour All Cards rule which requires merchant acquirers to ensure that Visa traders accept all Visa cards (see paragraph 2.66).

The MSCs charged by Barclays for Connect and other Visa debit cards; complaints made by traders

2.82. The main complaint made was that Barclays had asked traders to accept the same MSCs and percentage basis of charging for Connect as for Visa credit cards, whereas traders saw Connect primarily as an alternative to cheques, for which the clearance charges they paid to the banks were on a flat rate basis. The effect of Barclays' proposal would have been that traders would have paid much more for accepting Connect than they did for accepting cheques. Barclays had tried to force such higher charges on traders by threatening to terminate their agreements covering credit and all other Visa cards if they did not accept. While traders welcomed the advent of debit cards, they thought it unreasonable that they should be forced to accept Connect on the basis of an agreement drawn up a long time ago for credit cards, which served quite a different purpose. They argued that Barclays had been able to act as it did because of the Visa Honour All Cards rule (which had hitherto provoked no opposition from traders), because Barclays was the only Visa merchant acquirer in Great Britain, and because of Barclays' dominant position in the credit card market.

2.83. Because of the widespread refusal of traders to accept its terms, Barclays agreed, in the middle of 1987, to change the basis of charging to a flat rate, and had reduced the MSCs, but only to levels which were still higher than traders generally paid for clearance of cheques. Charges for cheques were said by some traders to be in the range of 10 to 30 pence per item; small and medium-sized traders generally paid two or three times more for Connect than for cheques.

2.84. The Commission received further complaints from traders in 1988. These arose because Barclays had by then told those traders who refused to accept the Connect card that, if they did not do so, their agreements would be terminated, in accordance with the rules of Visa. Complaints received by the Commission from six of the traders concerned showed that four had been offered MSCs in the range of 18 to 21 pence per transaction, one of 11 pence and the highest of 33 pence.

2.85. Traders also complained that, whereas the United Kingdom Visa banks competed with each other in the charges made for clearance of cheques, they would not be competing with each other so far as charges for Visa debit cards were concerned, because there was only one Visa merchant acquirer in Great Britain. Because the No Discrimination rule applied to Visa debit cards, traders could not encourage customers to use other means of payment by offering discounts. Their concern was increased by Lloyds' decision to issue a Visa debit card, under the same arrangements.

2.86. Traders suggested a number of safeguards or remedies, including prevention of debit cards being issued under the Access and Visa trade marks; separation of agreements between merchant acquirer and trader for credit cards from those for debit or other cards; and exemption of Visa debit cards from the No Discrimination rule.

The complaint made by Sainsbury's

2.87. Sainsbury's told the Commission that it wanted to offer customers the facility of the Connect debit card in its food supermarkets. Although it felt that the standard MSC offered by Barclays was not appropriate to a debit card, it was prepared to see an agreed charge per transaction expressed as a percentage per sale. However, Barclays had said that, because of the Honour All Cards rule, Sainsbury's would then be obliged to accept all other Visa cards, including credit cards. Sainsbury's did not wish to offer credit cards within its supermarkets because it thought the MSC offered to it for Visa credit cards was too high. (It had negotiated acceptable MSCs for Visa credit cards at its petrol stations and Homebase DIY stores.) Sainsbury's pointed out that traders who accepted the Switch debit card were under no obligation to accept any of the credit cards issued by the banks which issued Switch cards.

Discussions with the credit card operators

2.88. We discussed a number of matters arising out of these complaints and possible methods of dealing with them with Barclays and Visa; and some matters also with TSB, the only bank other than Barclays then acting as a Visa merchant acquirer, and with Lloyds, the only other bank issuing a Visa debit card, at the time when the complaints were being considered by the Commission. Their views are set out in the following paragraphs.

Barclays' account of its negotiations with traders on MSCs

2.89. Barclays told us that Connect offered traders advantages over cheques, including guaranteed payment in excess of the £50 cheque guarantee limit, quicker handling of transactions at the point of sale and in traders' office systems, and quicker crediting to a trader's bank account (if payment were made into the branch holding that account). It decided to charge traders the same MSCs as for Visa credit cards, and on the same percentage basis, because it considered that the benefits which traders would obtain were fairly similar, and that some of its costs were related to the value of the transaction. Barclays did not accept that Connect was principally a substitute for the cheque; it fulfilled other important roles.

2.90. Barclays decided to launch Connect as a Visa card, first, to avoid the substantial cost of recruiting a new network of traders and negotiating new agreements with them. Second, the Visa system was familiar to traders and cardholders. Third, the Visa trade marks gave the card international acceptability. Once it had decided to issue Connect as a Visa card, traders were contractually bound to accept the card under the terms of their agreements with Barclays, which had introduced a new form of merchant agreement in 1985 in which the definition of a `card' was widened to include `[any] other card approved by the Bank from time to time'. This condition reflected Barclays' own obligation to enforce Visa's Honour All Cards rule.

2.91. Barclays told us that many traders acting individually, or through trade associations or other bodies, argued that a debit card would be generally used as an alternative to a cheque, and therefore that the charge for Connect should be at a specific rate per transaction as with cheques. Because of the importance of the Connect project, Barclays had, in the negotiations following the launching of Connect in April 1987, accepted these representations, as an exceptional measure, whilst maintaining that in principle a percentage charge was appropriate.

2.92. Barclays told us that it had had to enforce the Honour All Cards rule, finally, in the second half of 1988, partly because of concern at its non-enforcement expressed to it by Visa and by Lloyds. Only a handful of traders had objected strongly to the MSCs finally offered, and only two very small ones had refused to accept them, so that Barclays had had to terminate their agreements. It had been very reluctant to take that step, but argued that the advantages arising from the rule far outweighed the disadvantages, which were not such as to justify removing the rule; that would have disastrous consequences.

2.93. We suggested to Barclays that the MSCs for Connect and other Visa debit cards should be reduced to levels nearer to the banks' charges for clearing cheques. Barclays replied that, in the bargaining which had followed the launch of Connect, the MSCs had been reduced. By December 1988 the vast majority of MSCs charged in Great Britain were in the range of 10 to 30 pence per transaction, with an overall average of about 16 pence, which was about one- quarter of the rate for Visa credit cards. It was still higher than the average for cheques, which Barclays considered justified by the additional advantages given to traders by debit cards over cheques.

2.94. In Northern Ireland very little business was generated by debit cards. Barclays told us that the MSC for most traders was (in February 1989) 30 penceexcept for branches of traders in Great Britain, which used the rate negotiated for the group as a whole. TSB told us that it had decided to use the existing rate applying to all Visa cards, rather than negotiate a separate rate for the very small number of transactions on debit cards.

Barclays' negotiations with Sainsbury's

2.95. Barclays told us that, with the continued reduction in costs from the application of electronic techniques to payments systems, it hoped to reach agreement with Sainsbury's on MSCs, so that Sainsbury's could accept all Visa cards; if so, the issue raised with the Commission would have been resolved.

Barclays' position as a monopoly supplier of credit card services

2.96. We suggested to Barclays that its actions both on MSCs for Connect and other Visa debit cards, and with regard to Sainsbury's, were also steps taken for the purpose of exploiting its monopoly position as a supplier of credit card services in the United Kingdom. As regards the MSCs, Barclays argued that, if someone else had issued the first Visa debit card, the same problems would have arisen. The economic power of traders had forced Barclays to modify radically its original proposals for MSCs, showing that it did not have the power to disregard customers' views. So far as Sainsbury's was concerned, Barclays replied that the Honour All Cards rule required it to give the response it did, irrespective of its market share in credit card services.

Comments by Visa, Barclays and TSB

2.97. The following paragraphs summarise the views of Visa, Barclays and TSB, as indicated.

The Honour All Cards rule and its effects on competition in the United Kingdom

2.98. Visa argued that the rule was a fundamental provision which underpins the key attribute of a Visa card: its acceptability on a world-wide basis. Cardholders and traders benefit from this universal acceptability: cardholders have a payment instrument they can use world-wide and traders know that they can accept a Visa card from any cardholder and, provided the correct procedures are followed, will receive prompt and guaranteed payment from their merchant acquirer. Withdrawal of the Honour All Cards requirement from United Kingdom Visa traders would lead to a complete breakdown of the system in the United Kingdom; it would also have adverse consequences on an international scale as foreign cardholders trying to use those cards in the United Kingdom would find their Visa cards refused. Even a small number of refusals by Visa traders to accept Visa cards would rapidly undermine cardholders' faith in the Visa card and destroy its status as a mass payment methodcardholders could not be sure whether their cards would be accepted or not.

2.99. Visa argued that certainty of acceptance was important for any payment instrument. In the Visa system because of the separation of card-issuing and merchant-acquiring functions and because of members' freedom to provide whatever financial services they wished via the Visa card, the Honour All Cards rule meant that traders had to accept cards issued by members other than their merchant-signing members and which could be providing the cardholder with any one of a limitless range of financial services.

2.100. Within the context of a system like the Visa system which enables its numerous organisations to issue Visa cards and sign Visa traders, the rule promoted competition because it enabled smaller financial institutions which could not themselves establish a domestic or international payment card operation to offer a card accepted on a huge scale throughout the world. By providing guaranteed acceptance of cards, the rule removed one of the largest potential barriers to entry into the consumer payments market: the restricted appeal of an instrument which is not widely accepted. Similarly, it offered each Visa merchant acquirer, irrespective of the number of cards it itself had issued, a pool of over 190 million cardholders world-wide. This widening of competition and potential competition promoted choice, improved terms and the development of new products and services.

2.101. Members' freedom to provide whatever financial services they wished via their Visa cards was another characteristic of the system which had increased its appeal and which was beneficial for participants in the system as well as the public interest. It increased the appeal of the card by allowing Visa issuers to develop a large variety of commercially successful payment services and promoted competition by facilitating the introduction of many `products' (cards providing different services) which could compete within the Visa system and with other modes of payment within the consumer payments market as a whole. Competition took place at two levels: between the Visa system and other international and domestic payment methods or systems (including MasterCard, American Express, Eurocheques, Switch, and store cards), and between individual Visa members, who were in competition with each other as well as with the suppliers of other methods of payment. This increased competition encouraged choice, innovation and the acceptability of cards to cardholders and traders, leading to economies of scale.

2.102. As regards the question of competition between debit cards and credit cards, Visa objected that it was artificial and unrealistic to classify cards into separate categories of credit cards and so-called debit cards, particularly in the context of the Visa system where issuers could provide whatever financial service they chose via their Visa cards. A very large number of different services were provided by Visa issuers, many of which could not be classified as traditional `credit card' services nor `debit card' services. That having been said, Visa argued that there was no support for a suggestion that the introduction of debit cards under the Visa system had led or might lead to there being significantly less competition between debit and credit cards in the United Kingdom than if debit cards were issued outside the Visa system. Visa did not believe that there would be any significant reduction in the number of Visa trader outlets because of any reluctance to accept the large numbers of new debit cards recently issued in the United Kingdom by Visa members. On the contrary, Visa believed that the addition of the Visa trade mark to any plastic card enhanced the appeal of that card, would increase the number of cards issued and the volume of business transacted by Visa card, thereby rendering Visa cards more attractive to Visa traders. Visa said that although it knew that objections had been raised by traders when Barclays introduced its Connect card, it understood that there were now virtually no problems concerning the honouring of all Visa cards by existing Visa traders. It also said that, overall, Visa was gaining, not losing, traders in the United Kingdom.

2.103. Visa told us that its rules did not prevent members issuing cards under systems other than the Visa system, or issuing their own cards. Prospective debit card issuers, and traders, could choose from a range of possibilities, including cards issued under the Visa, MasterCard or Switch systems, retailers' in-house schemes or issuers' proprietary schemes and, possibly, in the future cards issued under the system now under development by EftPos UK Ltd. Visa believed it would be anti-competitive to prevent Visa members from issuing debit cards under the Visa system because it would reduce the options open to its members.

2.104. Visa considered that criticisms of the Honour All Cards rule from traders who did not accept Visa cards were essentially criticisms of the level of MSCs which they were being offered. In its view, what was at issue was not so much the terms on which so-called debit cards were to be accepted but, rather, the terms under which the new electronic payments systems were in due course to be introduced. When this new technology became widespread far more purchases would be made with plastic cards, including debit cards.

2.105. Barclays and TSB argued that the rule was a fundamental provision designed to promote the universal acceptability of all types of Visa cards and an acceptable payments system, which operated throughout the United Kingdom and internationally, with advantages for both traders and cardholders. Withdrawal of the ruleleaving traders complete freedom as to which Visa cards they acceptedwould lead to a complete breakdown of the system in the United Kingdom; cardholders would never know whether their cards would be accepted or not.

2.106. The rule promoted competition in that it enabled financial institutions throughout the world, which could not themselves establish an international payment card operation, to take part in such an operation, while leaving them free to fix their own terms with cardholders and traders. It was therefore fundamental to the large growth in numbers of cards issued and traders signed which had taken place. There was competition between Visa members and with other international payments systems, in particular MasterCard/Eurocard and American Express. TSB drew our attention to the fuller statement of its views on the Honour All Cards rule in paragraphs 6.267 and 6.268.

2.107. Barclays and TSB also argued that there was no evidence to suggest that the application of the rule had led or might lead to any significant reduction in competition between debit and credit cards in the United Kingdom or that many traders would take the line that Sainsbury's was taking; most of its competitors in food supermarkets accepted all Visa cards. There were also other debit cards which Sainsbury's could accept, such as Switch. TSB pointed out that, since Sainsbury's did not accept credit cards in its food supermarkets, debit cards would not in any event be in competition there with other cards or methods of payment. If other traders adopted the same position as Sainsbury's, Visa cards, both debit and credit, would be less widely used, and competition would to that extent be curtailed.

2.108. Barclays did not accept our suggestion that its actions over Connect had restricted competition between debit and credit cards in the United Kingdom. All but two very small Visa traders had accepted Connect and other Visa debit cards. By launching Connect, Barclays had stimulated other banks to launch competing cards. Lloyds had subsequently issued a Visa debit card, and TSB had announced that it would do so. NatWest, Midland and RBS had begun to issue Switch debit cards.

2.109. Barclays also pointed out that the French competition authorities had recently held inter alia that, in the absence of the Honour All Cards rule, the development of plastic cards might be restricted, and that the rule was therefore essential for economic progress.[1]

2.110. Visa, Barclays and TSB all argued that there would soon be additional Visa merchant acquirers competing with Barclays: Sainsbury's (and other traders who adopted a similar position) might be able to reach agreement with one of them. The increase in competition between merchant acquirers within the Visa system and by suppliers of other systems and the growth in the use of electronic methods of payment could both be expected to reduce MSCs. Barclays also argued that the prospective introduction of EftPos would lead to an increase in the number of debit cards which traders could accept without having to accept credit cards.

2.111. We were told that the number of debit cards already issued was considerable and growing strongly. Barclays advised us that 1.86 million Connect cards were in circulation at the end of March 1989. By the end of April 1989 Lloyds had issued just over 1 million Visa payment (debit) cards. Visa, Barclays and TSB said that the general expectation was that some holders of debit cards would use them in preference to credit cards.

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[1] Décision no 88-D-37 du Conseil de la concurrence relative au Groupement des cartes bancaires `CB', published in the Bulletin Officiel de la Concurrence, de la Consommation et de la Répression des Fraudes, on 15 October 1988.

Possible effects of preventing the Honour All Cards rule being applied to Visa debit cards in the United Kingdom

2.112. Visa pointed out that its members had complete freedom as to the type of financial services offered via their cards and there was therefore no identifiable sub-category of `Visa debit cards'. There was no definition of a `debit card' within the Visa system nor, indeed, was there a generally accepted definition of the debit card outside the Visa system. Increasingly, plastic cards were being used to offer a range of services to cardholders. Moreover, it was possible for a single card to give the cardholder a choice of payment methods; the cardholder could choose the particular payment method to be used for each transaction by means of the personal identification number or sales voucher used (for example, choosing between immediate debit from an account, a 20-day grace period then direct debit, or a revolving credit facility).

2.113. Visa said that some United Kingdom Visa issuers had issued cards other than `traditional' revolving credit or charge cards before Barclays launched its Connect card. United Kingdom traders had always had to accept Visa cards from foreign cardholders, and a large number of Visa cards issued outside the United Kingdom were not traditional credit or charge cards. In many countries, cards linked to bank accounts comprised the majority of Visa cards issued. Until the launch of Connect, there had been no suggestion that the level of MSCs paid should depend on the arrangement between the cardholder and the card issuer, nor that a Visa trader should be able to refuse to accept some Visa cards.

2.114. Visa said that a simple alteration of the Honour All Cards rule would not be enough to enable certain United Kingdom traders to accept Visa debit cards. In particular, this objective could not be achieved by declaring that the Honour All Cards rule should not apply to Visa debit cards used in the United Kingdom, or to Visa debit cards issued and used in the United Kingdom, as the Commission suggested.

2.115. If the Honour All Cards rule were withdrawn from Visa debit cards, that would mean only that existing Visa traders need not accept Visa debit cards. This was not a realistic commercial position. Apart from the practical problem that one could not tell from the face of a Visa card whether it is a so-called `debit' card or not (see the following paragraph), any rule change which permitted refusals of Visa cards at the till would completely undermine the Honour All Cards principle, with the consequences already described. In any case, such a rule change would not assist any trader like Sainsbury's which said that it would like to accept Visa debit cards but not any other sort of Visa card. As argued in paragraph 2.104, Sainsbury's real concern was not the type of financial service provided via a Visa card (which was of no direct relevance to traders) but the level of MSCs applied to Visa cards.

2.116. Visa explained that Visa debit cards were not readily identifiable from other Visa cards because Visa issuers had complete freedom as to the services they offered via their cards and were not required to indicate anywhere on their card the type of service provided. Traders would therefore be unable to identify Visa `debit cards' unless a definition was laid down and rules developed enabling cards meeting this definition to be identified; this was not a commercially viable alternative. Visa argued that any changes to the present system could not practicably be applied to all 20,000 or more Visa issuers world-wide. It would in any case be wholly disproportionate to the apparent size of the problem complained of in the United Kingdom. Visa stressed that, quite apart from the practical question of how debit cards could be distinguished from other payment cards, it needed to prevent the serious damage to the Visa system which would result if merchants were able to refuse to accept `ordinary' Visa cards.

2.117. If United Kingdom law were changed so as to prevent Visa debit cards benefiting from the Honour All Cards rule, the immediate consequences of such a change to that rule would be that:

(a) to avoid total confusion in shops, and grave damage to the Visa system, as traders tried to identify `debit cards' and refuse them, all existing Visa cards meeting the definition of `debit cards' would have to be withdrawn;

(b) the strength of the Visa system would be reduced by the loss of present and future cardholders and card usage and the resulting opportunities for development and economies of sale; and

(c) competition within the Visa system would be reduced and competition offered by the Visa system in the field of debit cards to other card systems (such as Switch) would disappear. Smaller Visa issuers in particular would be likely to find their opportunities for competition reduced.

Visa members and Visa itself would need to consider developing an alternative system dealing with debit cards only; it could not be assumed that they would be prepared to do that. If the proposal was that debit cards used in the United Kingdom (as opposed to cards issued and used in the United Kingdom) should no longer benefit from the rule, Visa would have to consider rule changes affecting the many thousands of Visa card issuers world-wide. Again, change on this scale would be wholly disproportionate.

2.118. Barclays pointed out that, in addition to `traditional' revolving credit cards, traders in the United Kingdom had long accepted Visa Premier cards issued in the United Kingdom, which were charge cards. They had also accepted debit cards, or other types of cards linked to bank accounts, issued in other countries, and at the same MSCs as for credit cards.

2.119. Visa told us that it exercised no control over the level of MSCs paid by its members, nor did it collect information about the levels of MSCs. To the best of its knowledge, in most countries there was one standard rate of MSC for all Visa cards, although in Scandinavian countries a distinction was made between foreign and domestically-issued or -usable cards and in Sweden also between domestic credit cards and debit or branch account- linked cards. The international interchange fee (Issuers Reimbursement Fee) was applied to all Visa cards which have been used outside their country of issue and thus applied to all foreign-issued Visa cards used in the United Kingdom, whatever the financial arrangements between the cardholder and the card issuer, or the trader and the merchant acquirer.

2.120. Barclays also argued that it would be impracticable to operate an arrangement under which the Honour All Cards rule (or the No Discrimination rule) was not applied to Visa debit cards used in the United Kingdom, or only to Visa debit cards issued and used in the United Kingdom, as the Commission had suggested. It was difficultand would become increasingly difficultfor traders and their staff to distinguish between most debit and credit cards. Many foreign Visa cards were debit or deferred debit cards. Though traders were aware, because of the publicity, that the Lloyds Visa card and its own Connect card were debit cards, in practice there would be many Visa cards issued on different terms.

2.121. Barclays suggested that overseas Visa card issuers could not generally be expected to redesign their cards to distinguish between them in the way that would be needed if, as suggested by the Commission, the Honour All Cards rule was not to apply to debit cards; for that reason also, the Commission's suggestions were impracticable. To the extent that such arrangements could be introduced, it would undermine the benefits of the Honour All Cards rule to the particular detriment of foreign cardholders, who would become more important as time went on. Other unacceptable results could be produced. For example, if traders were allowed only to accept United Kingdom-issued Visa debit cards (together with all foreign-issued Visa cards, of whatever type) but were free to refuse United Kingdom-issued Visa credit cards, that would favour foreign-issued Visa credit cards (some of which could be issued by foreign subsidiaries of United Kingdom banks) at the expense of United Kingdom-issued Visa credit cards.

Separate negotiation of MSCs for credit and debit cards

2.122. In response to our suggestion that the MSCs for credit and debit cards should be negotiated separately, and set out in a separate annex to the Merchant Agreement, Barclays responded that it had in practice adopted that solution, in that it now had one MSC for all Visa debit cards issued in the United Kingdom, and another MSC for all other Visa cards at present issued in the United Kingdom or abroad. It would follow that policy if a new card, requiring yet another different charging structure, were to be issued. TSB argued that separate formal agreements would not be possible unless the Honour All Cards rule were abolished, but that the present system allowed for different pricing for credit cards and for debit cards. In its new Retailer Agreement Lloyds provides for a separate charge to be made, on a flat rate basis, for debit cards (Visa and other) as distinct from credit cards.

The application of the No Discrimination rule to Visa debit cards used in the United Kingdom

2.123. In response to the Commission's suggestion that the No Discrimination rule should not apply to Visa debit cards used in the United Kingdom, Visa said that it did not see how the suggestion related to the supply of credit card services: allowing Visa traders to discriminate against debit cards (if this could be implemented within the framework of the present Visa systemsee the following paragraph) would simply allow existing Visa traders to decline to accept or to discriminate against Visa debit cards. It reiterated that it would be illogical to draw a distinction between debit cards and any other type of payment card as regards the No Discrimination rule. It objected to the suggestion that the No Discrimination rule should be removed as regards debit cards on the same grounds as it had objected to the similar suggestion in relation to credit cards and it referred to its comments on that suggestion (see paragraphs 6.71 to 6.80).

2.124. Visa said that on practical grounds the Commission's suggestion could not be implemented by means of a simple order that the rule should not apply to Visa debit cards. For the reasons set out in paragraph 2.116, it would be necessary to determine a definition of `debit card' and introduce special rules making such cards readily identifiable. As a practical matter this could be done only at United Kingdom level thus enabling traders to discriminate against all debit cards issued by United Kingdom issuers and used in the United Kingdom, but not against all Visa debit cards used in the United Kingdom.

2.125. Visa told us what the effect would be if the No Discrimination rule were declared inapplicable to United Kingdom Visa debit cards, without any restriction being placed on the amount of surcharge or discount which could be applied. If Visa took no steps to limit the damage, its system would suffer as a result of Visa traders being able effectively to refuse Visa debit cards by applying very large surcharges to them. Again, change to the system on the scale required would be wholly disproportionate and not in the public interest.

2.126. Visa argued that if Visa debit card customers were surcharged by traders, this was likely to make Visa debit cards less attractive to customers and reduce competition between Visa debit cards and all other methods of payment, including credit cards and non-Visa debit cards. That might weaken the competition provided by debit cards as a whole to other methods of payment.

2.127. TSB referred us to its comments on the suggestion that the No Discrimination rule should not be applied to credit cardssee paragraph 6.240.

Lloyds' comments

2.128. Lloyds argued that debit cards did not appear to fall strictly within the terms of reference for the inquiry. Although the terms of reference did not deal expressly with the position of debit cards, it submitted that, taking the reference as a whole, the expression `credit cards' was intended to be narrowly construed and did not embrace debit cards; and that the definition of `charge cards' (which were expressly excluded from the reference) was sufficiently wide to cover debit cards. It went on to argue that issues such as whether the No Discrimination rule should not apply to the acceptance by traders of Visa debit cards did not strictly arise for consideration by the Commission.

2.129. As regards the MSCs for debit cards, Lloyds argued that those cards provided greater benefits to traders than did cheques, such as a higher level of guaranteed payment and faster handling of transactions; a direct comparison between MSCs for debit cards, and the banks' charges for cheques, was therefore inappropriate. Furthermore, the concern expressed by traders that the banks were not competing with each other on MSCs for debit cards no longer applied. Lloyds began to compete with Barclays, as a Visa merchant acquirer, in March 1989; it expected other banks to compete similarly before long.

2.130. Lloyds argued that the distinctions between credit cards, debit cards and charge cards were illusory. Debit cards might be linked to an overdraft facility and therefore competed with credit cards in relation to the supply of credit. They also competed as a payment medium. The primary difference was the absence of an interest-free period but changing market conditions might force credit card issuers to reduce the interest-free period or to impose a charge for credit cards. Charge cards were often linked to overdraft facilities and thus could be considered either as a credit card for which a fee was charged or a debit card with delayed debiting to a current account.

2.131. Lloyds did not consider that the No Discrimination rule was an obstacle to the introduction of debit cards; indeed it facilitated their introduction by removing the possibility of surcharges being made on transactions paid for with debit cards. Very few traders appeared to be refusing to accept Visa debit cards.

MISCELLANEOUS MATTERS

APRs for credit card borrowing

2.132. TSB argues (see paragraph 6.248) that, because of the way in which the APR is calculated, under the requirements of the Consumer Credit Act 1974, it does not take into account the interest-free period which purchases attract, and produces an accurate representation of the cost of borrowing for only a small number of customers.

2.133. The purpose of the APR is to provide a standard measure to help consumers to compare one type of credit with another and one trader's terms with another; for that to be possible, the APR needs to be calculated using a standard format. We show, however, in Table 3.16 and paragraph 3.67, the effects of the interest-free period on the relationships between the amounts of interest paid and the amounts of credit outstanding, for different categories of credit card borrowers. We understand that credit card operators can publish illustrations of the differing rates of interest paid in different circumstances, provided that their advertisements comply with the Advertisements and Quotations Regulations made under the Consumer Credit Act.

2.134. TSB also argues (see paragraph 6.263) that charging a fee for a credit card would alter the basis on which the APR was calculated, and lead to the quotation of a misleadingly high APR. We observe that that does not appear to have been a problem for American Express, on launching in the United Kingdom its Optima credit card in March 1989. American Express quoted an APR for the actual borrowing, and other APRs reflecting also, as required by the Consumer Credit Act, the cost of its membership and annual fees which need to be taken into account (see paragraph 3.111). The OFT has advised us that the introduction of a fee for the card need not lead to the quoting of a misleading figure for the APR.

The cheque guarantee limit

2.135. Some of those who gave evidence during the inquiry commented on this subject. The cheque guarantee limit set by the banks can influence the extent to which cheques compete with credit cards as methods of payment for goods and services obtained from traders. The cheque card limit remained unchanged, at £50, from 1977 until April 1989, when the banks agreed to introduce some flexibility into the scheme so that they could offer their customers £100 and £250 guarantee cards. The cheque card scheme, under which these limits are agreed, forms part of an overall agreement of the Association of Payment and Clearing Services (APACS), which is registered under the Restrictive Trade Practices Act. The OFT is currently considering the competition implications of the agreement.

2.136. Immediately prior to the April change, the DGFT expressed doubts not only about the £50 agreed level, but also about the need for any agreement on a limit. He said he would be concerned if there were no changes, or if arguments about the availability of other means of payment more profitable to the banks were a determining factor. After the April change the DGFT noted that the additional flexibility which had been introduced would increase competition amongst the banks, and that it was consequently less likely that he would find the cheque card scheme significantly anti-competitive. He added, however, that he was still under a duty to consider the implications for competition of the APACS agreement, including the cheque card limit, and to advise the Secretary of State whether it should be taken to the Restrictive Practices Court.

Use of the Access trade mark

2.137. We have noted the dispute which has arisen between Barclays and the JCCC about the use of the Access name and logo, which is being pursued through the courts. This may have some effect on future competition between Barclays and the Access banks, and the JCCC, as merchant acquirers. We note also the JCCC's comments on the use of the Access brand name, in paragraph 6.310, including its statement that it would be open to new MasterCard/Eurocard merchant acquirers to handle transactions generated by Access cards without having to use the Access brand name or the services of the JCCC.

No Discrimination rule

2.138. We have enquired about the position of American credit card operators under United States federal law, so far as this rule is concerned. We have found that, under the provisions of the Truth in Lending Act 1968,[1] credit card issuers in the USA may not prohibit other sellers from offering discounts to cardholders to induce cardholders to pay by cash, cheque or similar means, rather than by credit card. A prohibition on sellers, under that Act, which prevented them from imposing surcharges on cardholders who chose to use a credit card instead of cash, cheque or similar means, ceased to have effect on 27 February 1984.

[1] 15 USC 1601; 82 Stat 146; Pub L90-321 (29 May 1968), amended variously.