

Competitive Conditions Analysis on the Credit Cards, Debit Cards and Electronic means of Payment

Detailed Summary

1. Legal Framework

1. In Argentina, the Payment Cards Market is regulated by Act 25,065, modified by Act 26,010 in 2005, known as the "Credit Cards Act" (hereinafter the "LTC" for its Spanish acronym). The LTC establishes that the Central Bank of the Argentine Republic (BCRA for its Spanish acronym) and the Secretary of Commerce shall act as enforcement authorities under said legislation.
2. In Argentina, there are three different kinds of cards which can be used as payment methods: credit, debit and purchasing cards. The LTC stipulates that while credit and purchasing cards can be issued by a licensed financial institution, debit cards shall only be issued by banks authorized by the BCRA. Therefore, entry barriers for the issuance of debit cards are the same than entering the banking institutions market, being more economically burdensome than the barriers to enter the credit cards market.
3. Additionally, article 15 of the LTC regulates the merchant discount fee that shall be charged in every respect, setting a cap of 3% for credit cards and 1.5% for debit cards. Furthermore, the LTC stipulates that different fees shall not be charged "*among businesses acting under the same activity or offering similar products or services*".

2. Economic Analysis

4. The Electronic Payment System Market is defined by the economic literature as a *bilateral or two-sided market*.¹ Therefore, an Electronic Payment System not only provides services to two groups of clients (shops and cardholders), but also has a joint demand, since the service only is valuable if both sides of the market agree on using it.
5. This market involves several actors, technologies and fees for services. As a consequence, there are certain intermediate activities that make the transactions successfully, these include:
 - a. Banking services, from which the resources are withdrawn to execute the payments,
 - b. Credit cards (and other means of electronic payments) issuance,
 - c. Electronic payment authorizations processing,
 - d. Acquiring: the activity through which the acquirers affiliate businesses to the electronic payment system. The acquirers are also called "Administrators" or "Licensees", since they need to sign a contract with the credit card's brand owner to operate in their name.
 - e. Payment facilitation or aggregation: the aggregators provide payment services for online sales. The aggregator must sign a contract with an acquirer in order to process the payments.
 - f. Provision of systems and equipment for processing offline payments, known as "Points of Sale" (POS).
 - g. "Gateways": similar to the processing equipment but for online transactions.
 - h. "Merchants" or points of sale (physical or virtual), where the transactions take place. They are required to sign a contract with an acquirer or an aggregator in order to operate with a credit card brand.

1 Rochet, J.-Ch. Y J. Tirole (2006). "Two-sided markets: A progress report", The Rand Journal of Economics 35, pp. 645-667.

6. The system works as follows: the credit card brand owner (hereinafter the “CCBO”), grants licenses to issuing cards and/or acquiring merchants for a fee. A cardholder makes a purchase using a card, he or she pays the price of the product plus an additional fee to the issuer for holding or using (or both) the card. The latter transfers the payment to the acquirer minus the interchange fee. Finally, the acquirer transfers the payment to the merchant, minus the merchant discount fee. Thus, not the level of prices matters, but also its structure, that is, the proportion of the total price that is allocated to each side of the market.
7. Another crucial actor on the electronic payment system is the “processor”, who is in charge of giving connectivity and technological solutions to the payment card system. When the cardholder makes a purchase, the processor sends the purchase to the CCBO (Visa, MasterCard, etc.) and to the issuing bank in order to complete the transaction.
8. The payment system is said to be “closed” whenever the issuer and the acquirer are the same company (e.g. American Express); while it is “open” when the issuer and the acquirer different companies (e.g. Visa and MasterCard).
9. According to the BCRA, in 2015 there were 80 financial institutions in Argentina, 64 of which were banks. The biggest bank in Argentina is the (state-owned) Banco de la Nación Argentina and it concentrates 27% of the total deposits in the banking system. In addition, the 10 largest banks have 76% of the total banking deposits. All of them participate as payment card issuers.
10. In December 2015, there were around 72 million cards in circulation, 34.5 million were credit cards and the rest were debit cards. There are more than 50 institutions that issue payment cards in Argentina, which are divided in 2 groups: (a) bank issuers; and (b) non-bank issuers. Currently, there are six main credit card networks in Argentina. Four of them are owned or issued exclusively by banks (Visa, MasterCard, Credencial and Cabal), while the other two work in closed systems (Diners and American Express). Additionally, there are other credit cards at a local or regional level, some of them belong to banks (such as Tarjeta Naranja) and some others that also work as closed systems, are owned by retail stores (e.g., CMR Fallabella and Cencosud). Bank issuers work mainly with Visa, MasterCard and Amex and lead the market in terms of the number of cards issued and the value of the transactions. The credit card market leader is Visa, which represented 58 % of the total credit card transactions in 2015, followed by MasterCard (11 %).

I. Relevant Markets

11. A common factor among international legal precedents is the identification of two separate markets between the issuing and the acquiring markets. Moreover, this National Commission for the Defense of Competition (“CNDC” for its Spanish acronym) has found that electronic payment systems are formed by a combination of activities related with each other, as described in the following sections.

I.1 Issuance of Electronic Means of Payment Market

12. In Argentina, the issuance of credit cards is mainly done by banks. The two largest credit card brands operating in the country (Visa with 60% of the issued credit cards, and MasterCard with 15%) do not operate on their own, but they do so through banks who obtained issuing licenses. American Express is the only one company that issues credit cards through a non-bank entity, but it also issues credit cards through certain banks.
13. Due to the existing integration between banking services and card issuance in Argentina, both services shall be considered as part of the same market.

I.2 Acquiring Market

14. The acquirer is in charge of linking businesses with the payment and banking systems. Additionally, it is responsible for paying the businesses. In Argentina, it is a common practice

that the acquirer not only promotes the issuing cards to new customers but it also provides the technical means (networks or gateways) needed for processing transactions.

15. Visa's only acquirer is PRISMA MEDIOS DE PAGO S.A. (hereinafter "PRISMA"), who also plays the role of processor and POS terminals provider (under the brand "LAPOS"). Furthermore, given that PRISMA is owned by the main banks in Argentina, it exists a triple vertical integration (issuer+acquirer+processor). This is a main determinant of the market dynamic, since it accounts for 58% of total credit card transactions. On the other side, MasterCard also has a single acquirer: FIRST DATA CONO SUR S.R.L. (hereinafter "FIRST DATA"), who processes the payments and provides the POS equipment (under the brand "POSNET") too.
16. PRISMA (for Visa) and FIRST DATA (for MasterCard) determine the commercial conditions under which they offer the acquiring services to merchants. Currently, both companies charge the maximum fee allowed by the LTC to almost all economic activities. In the case of Visa, 95% (2.85 percentage points) of the merchant fee is transferred to the issuing bank as interchange fee, while the other 5% goes to the paying bank. PRISMA does not receive a (direct) payment for its acquiring services. The allocation of the merchant fee between issuing and paying bank is determined by PRISMA. MasterCard's interchange fee is determined by MASTERCARD INTERNATIONAL and is similar to the one determined by PRISMA. The difference between the merchant discount fee and the interchange fee is divided between FIRST DATA and the paying bank.
17. Despite the dominance of this vertically integrated (issuance and acquiring services) business model, thanks to the technological improvement and the development of e-commerce, new companies have emerged that acquire merchants through Internet based systems, which operate as aggregators (companies that ensure safe online transactions, reducing risks for buyers and sellers). The most important in Argentina is Mercado Pago, followed by PayU, Todo Pago (owned by PRISMA) and PayPal. Aggregators need to operate through an acquirer in order to process payments. Thus, they depend on PRISMA, FIRST DATA or Amex processing platforms.

I.3 Electronic Payment Processing Market

18. Electronic transactions (regardless of who processes them) need to have access to the buyer funds (through an account or credit card financing at the issuing bank). Therefore, there are no alternative to processing institutions to complete a payment card transactions. As a consequence, this market is defined separately.

I.4 Provision of Terminals or Interfaces for Electronic Payment Market

19. This market is comprised by all the companies that offer interfaces and equipment to perform electronic payments in-store, called POS (Point of Sale). In Argentina, for in-person channel, these interfaces are offered by two companies, POSNET (owned by First Data) or LAPOS (owned by PRISMA). In the e-commerce market, this function is accomplished by the gateways (Decidir, owned by PRISMA and GlobalConect). Given the technological innovation, this market is potentially competitive. For instance, the development of the Near Field Contact or "contactless payment", which provides customers with an alternative to payment cards, for low amount purchases.
20. On the demand side, (composed by merchants that use electronic payment systems), the interface that connects them is an irreplaceable supply, so a different relevant market shall be defined as "Provision of terminals or interfaces for electronic payment market".

II. Analysis of Market Power in the Relevant Markets

21. PRISMA, through its associated companies, participates in the four relevant markets that have been defined, and in both channels of trade. In addition, PRISMA is owned by 14 banks,

who issued 80% of the credit cards and 72% of the debit cards currently in the market. PRISMA also participates in other payment systems like Pagomiscuentas and Banelco, where credit and debit cards issued under the Visa brand are used.

22. Regarding FISRT DATA, it participates in three of the four described relevant markets, since it does not participate in the Issuance of Electronic Means of Payment Market. Additionally, it has the only license for offering acquiring services to operate with MasterCard, which is the second most important credit card in Argentina and issued 40% of the total debit cards.
23. Considering the banks individually, the Herfindahl-Hirschman Index (HHI), measured in terms of cards issued, is low in the credit as well as in the debit cards market, 806 and 737 respectively. Nonetheless, the banks who are also PRISMA's shareholders represent 79.79% of issued credit cards and 72% of issued debit cards. The situation is different in the processing and acquiring markets, which in fact are vertically integrated in Argentina and concentrated in companies that operate credit card brands exclusively. The most important players are PRISMA, who is licensed to use the brand "Visa" and FIRST DATA, who is licensed to use the brand "MasterCard".
24. Since PRISMA is the only company offering acquiring and processing services for Visa electronic payments (representing 58% of credit card transactions), it follows that the low concentration level in the issuance activity does not replicate in the activities of acquiring and processing. Visa transactions can only be processed by PRISMA, who plays a dual role: (i) it acts as a payment processing agent for the banking entities that own PRISMA; and (ii) it is the only Visa acquirer in Argentina. In the case of MasterCard transactions the acquiring is in charge of FIRST DATA and the processing is channeled through said company, although some banks process their own transactions.
25. Regarding the in-person channel, the vertical integration reaches the provision of POS terminals. Internationally there is more independence between different stages of the electronic payment systems.
26. Whenever a purchase is made through the virtual channel, connectivity is obtained through gateways or platforms provided by aggregators, who offer a technological solution to make the payment, providing an "online substitute" for POS terminals.
27. As a consequence of the de facto exclusivity in the processing and acquiring markets, competition is severely restricted. This combined with the relative weight of Visa as an electronic payment method in Argentina leads us to conclude that PRISMA holds a dominant position in the acquiring and processing markets.
28. Regarding FIRST DATA, it has the only license for offering acquiring services for MasterCard transactions. However, its situation is different from PRISMA's because it is not vertically integrated with issuing banks, and its participation in the acquiring market is substantially minor. Therefore, we cannot conclude that FIRST DATA holds a dominant position in the acquiring market.

III. Entry Barriers

29. Three entry barriers were identified. Regarding the issuance and acquiring markets, the main barrier that in order to enter those markets, the brand owner or an authorized licensee shall grant a license. Additionally, brand owners require that licensees be financial institutions or entities subject to supervision by the BCRA.
30. On the other hand, Argentina's market outcome, where PRISMA is owned by the largest banks in the country, generates an entry barrier in the acquiring market for Visa, as those financial institutions that could apply for a license to acquire Visa and are not PRISMA owners, are relatively small, and therefore, unlikely to invest in the development of an acquiring network.

31. An additional entry barrier in this market is given by the small profit margins of the acquiring market. This margin is determined by the interchange fee that, in the case of Visa is set by PRISMA as equal to 95% of the merchant discount fee.

IV. Effects on Competition

32. As explained above, PRISMA holds a dominant position in the processing and acquiring markets on both virtual and in-person channels. Moreover, while PRISMA does not participate directly on the issuance market, the 14 banks that are its shareholders have 80% of the issued credit cards and 72% of the issued debit cards.

33. The current layout of the Argentine electronic payment system restricts competition on the acquiring and financing markets.

IV.1 Restrictions to Price Competition

34. In electronic payment systems, there are three main prices: the fee charged to the cardholder by the issuer, the interchange fee paid by the acquirer to the issuer, and the merchant discount fee paid by the merchant to the acquirer. The first is determined in a market where there are many competitors and concentration is low and, therefore, is competitive.

35. The merchant discount and interchange fees are calculated as a percentage of the transaction value. The merchant discount fee is fixed at the legal cap of 3% and 1.5% for credit and debit card transactions respectively for most economic activities. This is mainly due to:

- a. PRISMA's market power and the lack of competition in the acquiring market.
- b. High interchange fees, which do not allow a reduction on merchant discount fees since the acquirer profit margin is already low.
- c. The prohibition to discriminate prices based on the volume of the transactions stated in the article 15 of the LTC.

36. As a result of these features, Argentina has a high interchange fees as compared to other countries. This, in turn, results in high merchant discount fees. Moreover, the lack of variability among the merchant discount fees and the fact that they are fixed at the legal cap are signals of the lack of competition.

IV.2 Restrictions to Financing Competition

37. According to the information gathered through this investigation, competition among banks to offer financing conditions has been reduced since 2013, when financing conditions have been centralized by PRISMA, who determines the applicable interest rates. The financing conditions were implemented through a mechanism called "zero-interest" payments. Despite the name, an interest rate determined unilaterally by PRISMA was charged to merchants, who, in turn, added the financial cost to the price of the product. This arrangement cannot be analyzed without taking into account that the largest banks are PRISMA's shareholders.

38. This system implies a restriction to competition from other financing options such as account overdrafts and personal loans, among others. Since, as explained above, the price of the product includes financial costs, the alternative financing methods are charging a "double" interest, which generates an important competition disadvantage.

39. In such a way, it is desirable on the one hand to improve transparency in prices and interest rates to finance consumption; and on the other hand, to give merchants and consumers competitive financing options from different banks and financial entities.

IV.3 Restriction to Third-parties Competitors Operations

40. There is enough evidence to believe that PRISMA has offered discriminatory sale conditions in the processing and the acquiring markets to its competitors in the Provision of Terminals or Interfaces for Electronic Payment Market. This means an alleged abuse of dominant position in the processing and the acquiring markets to exclude competitors in order to restrict downstream competition.

V. Conclusions and Recommendations

41. PRISMA holds a dominant position in the acquiring and processing markets, which has constrained the normal development of these markets.

42. This dominant position might have enabled PRISMA to extend its market power towards the provision of terminals or interfaces for electronic payment, and towards the aggregators and gateways services, representing an alleged abuse of dominant position.

43. Furthermore, the fact that PRISMA is owned by the largest banks in Argentina might be a mechanism which facilitates the coordination of commercial policies regarding the financing conditions offered to customers for purchases through credit cards.

44. Given that the interchange fees are close to the merchant discount fees; the acquiring profit margin is low, what discourages new entrants in this market.

45. In view of the foregoing, this CNDC recommends:

- a. To the BCRA, to review the electronic means of payment legal framework towards the promotion of a more competitive market, particularly:
 - i. Establishing adequate conditions in order to promote entry of new players in the acquiring market. Specifically, creating the "Payment Institutions" figure and forbidding any exclusive agreements between brand owners and processors and/or acquirers.
 - ii. Promoting multi-brand acquiring, so that any acquirer might have access to licenses of all the cards they wish to represent.
 - iii. Establishing legal conditions to guarantee that an entrant in the acquiring market might hire the processing service from the incumbent in non-discriminatory conditions.
 - iv. Promoting a mechanism to reduce entry barriers in alternative means of payments.
 - v. Fostering competition on consumption financing by encouraging transparency and allowing the customer to differentiate between the price of the product and the financial cost.
- b. To the BCRA and the Secretary of Commerce, as enforcement authorities of the LTC, to propose the following legal changes:
 - i. Repealing article 15 first paragraph of the LTC to enable acquirers to price discriminate among merchants.
 - ii. Modifying article 15 of the LTC in order to empower the BCRA to regulate the interchange rate following international best practices.
 - iii. Establishing a mechanism to guarantee transparency of the financial costs in credit card transactions. It is recommended to evaluate the design of an alternative to force the payment to the merchant to be equal to the cash price of the product minus the merchant discount fee, excluding any additional discount, such as interests.

- c. Finally, considering the outcomes of this investigation, this CNDC recommends the Secretary of Commerce to open an investigation over PRISMA and its owners for alleged anti-competitive conducts under the terms of Act 25,156.