GREATER LANGLEY
CHAMBER OF COMMERCE

Credit Card Merchant Fees

Issue
Every year, $44 trillion dollars' worth of payments are made in Canada. Only 20% of this value is done with cash, down from 50% in the 1990s. This signals the growing reliance and importance of credit card and debit transactions, not only for consumers, but also for the businesses that rely on these methods to accept payments. However, at $5 billion per year, the current system has resulted in Canadian merchant businesses paying some of the highest credit card acceptance fees in the world, costs which trickle down to the consumer regardless of their payment method.

Background
Many of the businesses accepting credit card payments for goods and services are unclear on the inner workings of merchant services providers (MSPs). The current system has resulted in many businesses paying higher fees for credit card acceptance than necessary. Businesses are enticed to switch service providers on the premise of lower rates. However, as most businesses are unaware of the actual VISA and MasterCard rates - the actual Merchant Discount Rate (MDR) - they are misled to believe that a lower MDR results in savings on their actual credit card transactions. On the contrary, a lower than actual MDR means that the MSP is losing money on every transaction and, thus, has to recoup its losses through the card brand fee and/or non-qualified surcharges, which can vary substantially across different service providers.
The 3 Components to Credit Card processing:

1. Merchant Discount Rate (MDR): This is the base rate charged by the provider. Any rate below the rate VISA charges the MSP for processing one of its credit cards causes the MSP to take a loss on the transaction. In order to recoup this loss the MSP thus has to bump up the rates in 2. and 3.

2. Card Brand Fee (CBF) - 0.10% or more (the actual cost is 0.08% but is rounded up by most MSPs): This fee is used by VISA and MasterCard to advertise their brands, as well as to improve the stability of their networks

3. Non-qualified Surcharge (NQS) - 0.30% is the average value of this surcharge. However, it can vary greatly depending on the base rate offered by the MSP. Certain MSPs will undercut the Merchant Discount Rate (MDR) and then increase the Non-qualified surcharge (NQS) to make up for the loss they incur. Monies raised through this rate are used by major banks to promote their credit card programs and to pay for benefits

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received by credit card holders. The rate is also charged on keyed transactions, which are considered higher risk, as well as on all Infinite credit cards (i.e. Avion, Aeroplan, etc.)

In 2010, the federal government introduced a voluntary code of conduct for the credit and debit card industry in Canada aimed at alleviating issues of asymmetric information and flexibility. When this code of conduct is adopted by the MSPs, they are expected to:

- to ensure that merchants are fully aware of the costs associated with the acceptance of credit and debit card payments;
- to provide the merchant with increased pricing flexibility to encourage consumers to choose the lowest-cost payment option (i.e. clearly show all components of the total fees, as most credit card agreements do not allow merchants to use incentives to discourage the use of credit card or premium credit cards); and
- to allow merchants to freely choose which payment options to accept.

However, this remains a voluntary code of conduct and, therefore has been adopted only by a limited number of service providers. Its voluntary nature stands to undermine any real benefits to merchants these policy proposals may have. In a 2013 decision, which dismissed a complaint against two large credit card service providers, finding that they had not violated the Competition Act, the federal Competition Tribunal acknowledged the issues in the country's credit card payment system and called for a regulatory solution. They stated that despite finding that the MSPs had not violated the Competition Act, “"…we note that the Tribunal found that Visa's and MasterCard's conduct is influencing the price of credit card services in Canada upwards and having an adverse effect on competition. At the same time, the Tribunal felt that regulation of the industry would provide a more appropriate solution than any remedy that it could provide1.” Providing merchants with greater flexibility in choosing their MSPs and discriminating against more expensive transactions is seen as an OECD international best practice, a practice currently not allowed in Canada2.

In April 2015, the federal government released Balancing Oversight and Innovation in the Ways We Pay: a Consultation Paper, aimed at seeking comments on national retail payment systems. However, there has been no movement on this issue since then, or an indication of the actions the government plans to take post-consultation.

Recommendations
That the federal government:

1. Consult with the banking and financial services industry in changing from a voluntary to mandatory code of conduct, as introduced in April 2010 for the credit card and debit card industry in Canada, thereby ensuring that all parties are

required to abide by and comply with the existing code's guidelines for greater transparency, disclosure and flexibility

2. Provide merchants with increased pricing flexibility to encourage consumers to choose the lowest- cost payment option.
3. Work to better educate merchants on their rights and options to battle any informational asymmetry
4. Enact legislation requiring full disclosure by service providers of all costs associated with acceptance of credit and debit payment

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