



House of Commons
CANADA

Standing Committee on Industry, Science and Technology

INDU • NUMBER 018 • 2nd SESSION • 40th PARLIAMENT

EVIDENCE

Tuesday, May 26, 2009

Co-Chairs

**Mr. James Rajotte
The Honourable Michael Chong**

Also available on the Parliament of Canada Web Site at the following address:

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Tuesday, May 26, 2009

• (1530)

[Translation]

The Co-Chair (Hon. Michael Chong (Wellington—Halton Hills, CPC)): Good afternoon, everybody.

[English]

Good afternoon, everyone. Welcome to the joint meeting of the Standing Committee on Industry, Science and Technology and the Standing Committee on Finance.

I am here with my co-chair, Mr. Rajotte, who is the chair of the House of Commons Standing Committee on Finance. My name is Michael Chong, and I am the chair of the Standing Committee on Industry, Science and Technology.

Pursuant to Standing Order 108(2), we are studying credit card interchange fees and the debit payment system in Canada.

Today I am pleased to welcome two representatives of UseMyBank Services, Mr. Brian Crozier, co-founder of UseMyBank Services, responsible for global business development; and Mr. Joseph Iuso, who is the chief executive officer and also a co-founder of UseMyBank Services.

We're also pleased to welcome, from Moneris Solutions, Mr. Jim Baumgartner, president and chief executive officer; and Ms. Fern Glowinsky, senior vice-president, general counsel, and corporate secretary.

From TD Merchant Services, we're also pleased to welcome Mr. Jeff van Duynhoven, who is the president of that company.

Welcome to all.

You now have a chance to provide some opening remarks. We'll begin with UseMyBank Services.

Mr. Brian Crozier (Co-founder, Global Business Development, UseMyBank Services): Thank you.

We'd like to thank the committee for the opportunity to present our view, as a Canadian online payment service provider, of the online electronic transactions business in Canada.

My name is Brian Crozier. I'm in global business development for UseMyBank Services in Toronto. I've been in the online payment processing business for over 12 years. My business partner and CEO of UseMyBank, Joseph Iuso, has worked for major Canadian banks for over 20 years. Joseph has extensive knowledge of the technical capabilities of the Canadian banking system, as well as all aspects of

security, transaction processing, the self-service arena of ATM POS terminals, as well as telephone and Internet banking.

UseMyBank is a Canadian online bank service provider for online merchants and billers. Our core technology provides an easy way for online merchants to transact in real time with their customers using online banking.

Consumers who use a merchant's online checkout may choose their online bank and make a purchase or pay a bill in real time. We launched our service in 2002 and have processed millions of transactions for Canadians, with a good funds rate of 99.99999%.

UseMyBank pioneered online payments several years ahead of the Canadian banking institutions. We were able to accomplish this by leveraging the existing online banking systems to perform real-time payments. We have since expanded our service to hundreds of banks across 10 countries. This real-world experience gives us at UseMyBank a global view of the best online payment practices, which we can share with committee members.

The business of making payments in Canada is largely controlled by a handful of financial institutions. Many believe this constitutes a monopoly that stifles competition, which is the very lifeblood of Canadian business. E-commerce is an important and growing part of the payment industry in Canada. Payments to online merchants and billers are now in the tens of billions of dollars, and many merchants and consumers would like to see more available choices when making these online payments.

There is very little competition in the Canadian payments market. There is a tradition of in-house sales of merchant services, with the largest payment processor, Moneris Solutions, being owned by two of the largest banks. Paymentech and Global Payment Systems have taken over the rest of the market where mergers were not allowed. So it's not difficult to understand why new independent businesses face an uphill battle to offer service.

Interac, Canada's near-monopoly debit network, as well as Visa and MasterCard, are in the business of processing online payments. We believe it's in our country's best interest to offer consumers a choice by having as many suppliers of online payment services in Canada as possible, thus ensuring the quality of service as well as fair market prices.

Since 1989, retailers in Canada have been accepting debit payments at point of sale terminals for pennies per transaction using Interac. In 2006, Interac launched Interac Online, charging merchants upwards of 2% or more per transaction.

Canadian online retailers and billers require a greater variety of options when accepting payments from their customers—more than the current four banks that Interac supplies. For example, the Canadian travel and airline business processes billions of dollars in transactions each year online. This industry currently finds itself between high credit card rates and Interac Online's position of placing them on a restricted list. These retailers are unable to accept direct payments from their customers using online banking.

Canada's clearing and settlement system is among the most efficient in the world. The Canadian Payments Association operates national clearing and settlement systems for all cheques, wire transfers, direct deposits, pre-authorized debits, bill payments, point-of-sale debits, and online payments. Transactions that are charged to credit cards are not cleared through CPA systems, thus the CPA rules don't apply to them.

UseMyBank has met with the CPA to bring them a better understanding of the need for alternative forms of online payments and the benefit that such technology offers Canadian e-commerce. The rules ultimately drafted on this measure excluded not only UseMyBank but many other innovative companies from participating in the Canadian payment sector.

From its initial launch, UseMyBank has made every effort to be an active participant in the payment processing industry. Both in Canada and abroad, we have ensured that our goals and objectives are heard and understood at the regulatory and legislative levels of the financial banking industry.

• (1535)

This same scenario has been replayed time and time again with every group that has been charged with the responsibility of governing the Canadian payment industry. Sadly, innovations that could offer Canadian merchants safe and cost-effective ways to build their online business are being stifled, while other countries begin to surge ahead of us in this sector. We believe that the banking system in Canada should have regulations that foster competition and innovation, similar to the telecommunications industry today, which is enjoying more services and lower prices as a result of allowing more competition to enter a market that was once a monopoly.

In 2006, the Bank of Nova Scotia became a defendant in a case brought before the Competition Tribunal. It was alleged to have illegally reduced competition in the online debit payments market. The bank won the case, but the plaintiff, GPay, without the cooperation of the defendant and other Canadian banks, was unable to remain doing business. GPay was our payment processor for Canada at that time.

At one time, Canada was number one for consumer adoption and usage of ATMs, POS terminals, debit transactions, and online banking. We are no longer number one, as many of these other countries have surpassed us. Since 2000, the banking industry has not been as responsive to changing market conditions and expectations. Their policies and tactics have attempted to restrict the market by manipulating the rules and regulations through lobbying the CPA, the CBA, and other government agencies.

It is possible for Canada to regain its lead in the payments industry. However, it requires an environment that rewards

entrepreneurs for creating the next big ideas and companies. We hope that the committee can help make this a more friendly and competitive market for online payment service providers and their millions of Canadian and global customers.

Thank you.

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. Crozier.

We'll now hear from Moneris Solutions and, I believe, Mr. Baumgartner.

Mr. Jim Baumgartner (President and Chief Executive Officer, Moneris Solutions): Thank you very much.

Thank you for the invitation to speak to the committee regarding the study of the credit and debit card industry in Canada. We appreciate the opportunity to appear before you and share information with you in support of your study.

I'm Jim Baumgartner, president and CEO of Moneris Solutions, and with me here today is Fern Glowinsky, our senior vice-president and general counsel.

Moneris Solutions is a Canadian-based payment processor with operations in Canada as well as the U.S. Our head office is in Toronto, and we also have offices in Sackville, New Brunswick; Montreal; Calgary; Vancouver; and throughout the United States. We've been providing credit, debit, and gift card acceptance solutions to merchants in Canada and the U.S. since December 2000. We process for approximately 350,000 merchant locations in Canada and close to 65,000 merchants in the U.S.

Moneris is a joint investment of the Royal Bank of Canada and the Bank of Montreal. We distribute our products and services to the market directly through various sales channels. Moneris employs approximately 1,800 people, the vast majority of whom are right here in Canada.

As our role in the industry tends to be the least understood, I'll take a moment to briefly describe what we do. First, we enable merchants' acceptance of electronic payments by providing and supporting the cardholder facing solution, which may be a stand-alone device at the point of sale or enablement of a cash register, gas pump, kiosk, or even a website. Second, when a card is swiped—or inserted, in the chip context—we route that transaction and the authorization request through the payment brands to the card issuer. They send back an authorization message that we deliver to the merchant so the merchant knows that the customer is authorized by the issuing bank to complete the transaction. Once the transaction is authorized by the card issuer, the merchant will finalize the transaction with the cardholder and send us a settlement file that prompts us to settle funds into the merchant's bank account for that day's transaction activity.

An important component of our business model is merchant underwriting. We bear the risk when the merchant does not deliver the goods or services that have been paid for in advance—for example, when a cardholder purchases an airline ticket and the airline goes out of business prior to delivering the flight—and in the cases of merchant fraud and non-compliance with payment brand rules.

We also provide reporting to enable the merchant to monitor their transaction activity for the purposes of operational and financial reconciliation, as well as fraud monitoring.

Another important element of our service is exception item management. This includes the tracing of individual transactions and mediating on behalf of the merchant in the case of a transaction being disputed by a cardholder.

As a whole, these components are the payment processing value proposition. Payment processing is often the last interaction or final impression between the merchant and the consumer in the shopping experience, therefore it has to be instant, always on, and easy to operate. It is critical in enabling cashflow, and therefore the merchant must receive funds when and where they want them and have certainty of payment. The finality of payment feature in today's uncertain times removes an element of credit risk from the equation, as well as the risk in handling large amounts of cash.

The payment processor also plays a leading role in the integrity and evolution of electronic payment networks. With the introduction of enhanced verification technology such as chip, data security standards such as PCI, or new card entry modes such as contactless, the processor must upgrade its infrastructure. These are no small tasks. They're very capital-intensive and complex undertakings that have helped Canada maintain one of the most ubiquitous, secure, and successful networks in the entire world.

As an industry, we're subject to the increasing liabilities associated with potential data compromises. A number of recent high-profile breaches in the U.S. have highlighted the threats posed to the digital infrastructure. The reality is that the cost of compliance and ensuring security within the payment system is continually increasing as the threat of breaches and fraud continues to evolve.

● (1540)

The Canadian payment processing market is highly competitive. Most of North America's top processors actively market in Canada. Significant established players regularly enter the market. U.S.-based merchant processors now control a significant percentage of the Canadian market. In addition, there's a robust reseller industry that offers even more choice to merchants. Our industry is forced to compete on price and innovation to maintain our market position. And at this point in the evolution of the payment card industry, card acceptance is roughly equivalent to the growth in the retail economy. It is essentially a zero-sum game, requiring each industry participant to strive to be the most relevant to its merchants. We negotiate fees with merchants directly.

In terms of merchant acceptance of cards, merchants have a choice about acceptance, and they do so because of the significant value they receive from electronic payments, including avoiding the costs associated with handling cash, reporting and reconciliation, finality of payment, speed and throughput at the point of sale, and increasing customer satisfaction by offering their customers a payment method of choice.

There has been much discussion about interchange, and as you may know, it is the fee that's paid by the payment processors to the card issuers. In our pricing model, it is a component of our cost of goods sold. Payment processors do not set interchange rates; we are

advised of them by the payment brands. Other components of our cost base include the assessment fees that are paid to the payment brands, as well as our operating infrastructure.

There has also been much discussion about the introduction of competing debit products in Canada. As payment enablers, we have to invest in the infrastructure to process new acceptance products from card issuers because we expect that at least some of our merchants will want to be able to accept the card their customer presents for payment. As a result, we must develop the technical acceptance capability, build business processes, commercialize, and inform and train the merchant. New products attract a greater compliance burden, greater wear and tear on our hardware, as well as additional risk and exception item management.

We hope our remarks have provided some helpful insights, and we look forward to answering your questions. Thank you again for the opportunity to be here.

● (1545)

The Co-Chair (Hon. Michael Chong): Thank you, Mr. Baumgartner.

Finally, we'll hear from Mr. van Duynhoven.

Mr. Jeff van Duynhoven (President, TD Merchant Services): Thank you, Mr. Chair. I appreciate the opportunity to appear before you today on behalf of TD Merchant Services.

Payment systems are obviously a complex topic, but I'm happy to do what I can to help explain the process and explicitly the role that a merchant acquirer plays within that system. In the simplest sense, as acquirers, we provide our customers with point-of-sale payment devices, the hardware that sits on the counter in a store, and we process payments on behalf of the retailer.

Major merchant acquirers, or payment processors, including TD Merchant Services, Moneris, Global Payments, Chase Paymentech, and Desjardins, provide essentially the same set of payment capabilities to merchants, but we compete with each other primarily based on two things: the quality of service we provide and the price we charge that merchant.

TD is the only Canadian bank that currently operates a merchant acquiring business. The reason for this is quite simple. We believe it is a relationship business and we appreciate having a direct relationship with retailers and business owners across Canada. In fact, more than 85% of my clients are also clients and customers of TD Canada Trust, illustrating this relationship aspect for us.

In terms of pricing, as the committee knows, interchange rates are set by the payment network companies—Visa and MasterCard—and they both make these rates available via their websites. Both have stated their intention to enter the debit market in Canada and have communicated the interchange rates associated with accepting those debit cards. Acquirers take these interchange rates, determine our own additional direct costs, and then develop a comprehensive fee structure that we present to merchants. The cost of interchange is by far the largest component of the merchant discount rate.

In the past, we presented costs to merchants via a simple, often all-in merchant discount rate—that is, the all-in cost a merchant would pay per transaction process. This was feasible as the interchange rate structure was simple at the time. The payment networks have since changed their interchange rate structures to a more complex model that has different rates for consumer, premium, and business cards, as well as for online or other card-not-present transactions. As a consequence, acquirers also revisited pricing approaches to merchants.

TD Merchant Services completed this task in time for the introduction of Visa interchange rates in April 2008, and this was a significant effort and was completed at considerable cost to my business.

This committee has heard testimony to date regarding transparency on the part of acquirers. As part of our submission to today's hearing, we provided the committee with samples of notification letters that we sent to clients to illustrate the approach we take to articulate any change in the merchant's processing costs. I'd like to highlight to the committee, as well, that these letters are from 2007 and 2008, before Parliament began its studies on this matter. Quite simply, it's the way we do business.

As illustrated in these letters, we introduced new fees or changes to current fees arising from the interchange rate structures made by Visa, and we provided appropriate examples to ensure that merchants understood the impact of these changes. At TD Merchant Services, we are proud to provide our merchants with what we believe is a clear and transparent statement of their monthly activity.

I've shared a sample of this statement with the committee and have highlighted the Visa discount rate adjustment box, which lists the number and dollar amount of all transactions for which a rate in excess of the merchant discount rate has been applied. This section of our statement also clearly identifies the type of card used—for example, an Infinite card or a commercial card—in plain English, not via the use of codes or other more obscure terminology. This section also identifies the increase in the rate associated with the processing of these transactions and the sum of the additional charges for each card type processed by that merchant.

To reiterate, I know some organizations have complained that there is a lack of transparency at some points in the payment process. From my perspective, I believe that clients of TD Merchant Services have a clear picture of the fees they are paying for the transactions we process on their behalf. In fact, delivering quality service and communicating with customers in a clear and transparent manner is a key tenet for both TD Merchant Services and the entire TD Bank Financial Group.

• (1550)

As an acquirer, TD will continue to bring the latest payment options to our merchants. However, as these options are introduced, history would suggest that in order to be viable, any innovation needs to create value for all stakeholders in the payment value chain, whether they be issuers, consumers, merchants, or acquirers, as without the acceptance of all of the parties involved, these innovations are likely to fail.

As change evolves, we will continue to consult with our customers, presenting new options to determine whether they are of interest to them, as well as educating and training their staff on how to use the new technologies. Throughout this process, we will continue to communicate clearly so that merchants know exactly what they're paying for and that they're getting value for their money. As payment processes continue to develop over time, TD Merchant Services will not change our strategy of offering customer-focused, price-competitive, high-quality services to our clients in a transparent manner.

Thank you, Mr. Chair. I'd be pleased to answer questions.

[Translation]

The Co-Chair (Mr. James Rajotte (Edmonton—Leduc, CPC)): Thank you, Mr. van Duynhoven.

We have an hour and a half for questions and comments and we use both official languages so some MPs will ask questions in French and some in English.

[English]

So without further ado, we'll commence with Madam Coady.

Ms. Siobhan Coady (St. John's South—Mount Pearl, Lib.): Thank you very much.

Thank you for your very clear presentations this afternoon. I appreciate the time you've taken to present to this joint committee.

I have a series of questions I'd like to go through, so brevity would be asked, if you don't mind, just because there's such a lengthy list of questions.

I'm going to start with the credit card side of life and ask a couple of questions. Did you have any influence on the interchange fees at all? When Visa and MasterCard were making changes to the interchange fees—I think I know the answer, but I want to hear it from you—did you have any influence?

Mr. Jim Baumgartner: From our perspective, no.

Mr. Jeff van Duynhoven: I would say the same, no, not at all.

Ms. Siobhan Coady: When the changes were made to the interchange fees—I think TD has already indicated that they also changed their pricing model to merchants at the same time—did you see any increase being paid to you because of the changes in the interchange fees and then your change in pricing models?

Did you change your pricing model, Moneris?

Mr. Jim Baumgartner: Yes, we did.

Ms. Siobhan Coady: At the same time?

Mr. Jim Baumgartner: Yes, as the more complex interchange structure was introduced, we did change our pricing structure in response to that. I can tell you that overall from when we started the company—the first full year was 2001—to 2008, the difference between what we were charged in interchange and assessments and what we charge our merchants has come down. So what we call our gross spread in basis points has come down from 2001 to 2008.

Mr. Jeff van Duynhoven: In terms of the interchange rates?

• (1555)

Ms. Siobhan Coady: And your change in pricing model, how did that affect your business?

Mr. Jeff van Duynhoven: As I said, when the interchange changed from two rates to 21 on the Visa side, we had to look at our pricing. Some merchants did see increases, but others saw decreases as well, depending on which industry they were in, the types of cards they process, and how they process those cards. So we had customers who moved both ways.

Ms. Siobhan Coady: Would you say there was one particular industry that was affected more than others?

Mr. Jeff van Duynhoven: More from a transaction size, so those industries that had a higher transaction size benefited and those that had a low transaction size, like quick-service restaurants and those sorts of things, saw the biggest price increases.

Ms. Siobhan Coady: Would you say there's a big impact to your businesses on the premium card introduction in terms of price, negative or positive, any impact at all?

Mr. Jim Baumgartner: Well, it required a significant investment in infrastructure. Our system was not capable of handling the complex interchange structure that was traditionally more common in the U.S. When that was introduced here, it required an investment in the tens of millions of dollars to be able to handle that.

Ms. Siobhan Coady: Do you think the merchants bore any of that cost, or do you feel you bore most of it?

Mr. Jim Baumgartner: I'd say a combination of both, quite frankly. As I mentioned before, our spreads have come down since we started and so we definitely have borne some of it, but the merchants are paying more as well, and there's no doubt about it.

Ms. Siobhan Coady: In the interest of time, I want to move to the debit card side of things. There are a few questions I want to talk about. First of all, could you explain priority routing? Are you aware of priority routing?

Mr. Jim Baumgartner: On the debit side? Sure, I can, and I'll try to be brief. Cut me off if I'm not brief enough.

Priority routing refers to a practice where, if you had an Interac card today, and let's say Maestro was added to the card, the instructions from the issuers would be to route this through Maestro as opposed to an Interac transaction. The card brands have taken different approaches on this. Visa, more recently, has said that they're going to allow consumers to choose. MasterCard is asking the banks to indicate where they would like their customers' transactions routed through. So they've taken different approaches, as they will do occasionally.

Ms. Siobhan Coady: Have you been approached to program terminals to ensure either Visa or MasterCard? Are there any

inducements to ensure one priority routing or the other for either TD or Moneris?

Mr. Jim Baumgartner: In our particular case, Visa has offered us an incentive to develop Visa debit. However, we've not elected to roll it out yet because we're not comfortable right now that the price is appropriate for merchants. When MasterCard introduced the price for Maestro, we had some serious reservations about even offering it to merchants. But I have to give them some credit. They've since responded, I think, very favourably and have acknowledged that they're going to bring it down to the Interac levels, which obviously right now are virtually free.

Ms. Siobhan Coady: TD, would you like to—

Mr. Jeff van Duynhoven: We certainly talked to both card brands, and like Moneris, Visa had incented us to develop that capability. However, they've now also mandated acquirers as part of their operating regulations. We're subject to considerable fines if we actually don't support the Visa debit product.

But I would also like to add that it is giving merchants choice. So merchants do have a choice whether they choose to accept Maestro, in the case of MasterCard, or Visa debit, in the case of that particular product.

Ms. Siobhan Coady: Can you describe that choice?

Mr. Jeff van Duynhoven: In our case, we will advise our customers. We believe in transparency, as I said in my opening statement, so we'll give customers the choice. They will know that they've signed up for Visa debit and what the costs associated with that are.

Ms. Siobhan Coady: I have one quick final series of questions. This is about shifting the risk on debit cards.

I've been advised—and I'm asking if your understanding is the same—that there will be a shifting of the risk with chip cards, meaning that merchants will be bearing more of the risk. I'm seeing nodding heads. Is that your understanding as well?

Mr. Jim Baumgartner: That's exactly right. Starting in October 2010, both card brands have announced what's called a liability shift. That is, if you went to a merchant with a chip card, you entered your PIN, and then said that it wasn't you, the merchant would be liable for that transaction if they don't accept chip transactions. That's done, presumably, to motivate the merchant to roll out the chip devices.

• (1600)

Ms. Siobhan Coady: So there will be costs borne by the merchant for accepting that risk, which could be huge. Even though your interchange fees and other associated costs would normally have covered that associated risk, now you're downloading it.

Mr. Jim Baumgartner: In some respects it's a bad thing for us, though, because if the merchant isn't able to honour the liability—the merchant processor, or us, or just business, for example—we end up absorbing that liability. So this particular rule is a very, very bad thing from the merchant perspective. It's more pro-consumer.

The Co-Chair (Hon. Michael Chong): Thank you very much.

Go ahead, Madam Glowinsky.

Ms. Fern Glowinsky (Senior Vice-President, General Counsel and Corporate Secretary, Moneris Solutions): I just want to say that it's not our downloading. The payment brands, Visa and MasterCard, have announced liability shift. It's something that's being done and we're part of it.

The Co-Chair (Hon. Michael Chong): Thank you, Madam Glowinsky.

Thank you, Mr. Baumgartner and Mr. van Duynhoven.

Monsieur Laforest.

[Translation]

Mr. Jean-Yves Laforest (Saint-Maurice—Champlain, BQ): Thank you, Mr. Chairman.

I want to thank the witnesses for being here today.

Since we do not have too much time, I will start with a specific request. Since you mentioned transparency, I want to ask you to be transparent.

My first question is for Mr. Baumgartner as well as Mr. Van Duynhoven. Could you provide us with a detailed list of all the fees charged to merchants by Visa, MasterCard and you, the acquirers? Are those fees fixed or are they a percentage of the value of the transactions? We have heard a lot about interchange fees, assessment fees, marketing fees and fees for foreign cards. Could you provide such a document to the committee? I am not asking you to answer now because it would take far too much time. Can you do that?

[English]

Mr. Jim Baumgartner: Yes, absolutely.

[Translation]

Mr. Jean-Yves Laforest: Very well.

Again, to both of you, are you charged direct fees by financial institutions for transactions processed by credit or debit cards?

[English]

Mr. Jeff van Duynhoven: No. We are charged fees by Visa or by Interac for processing transactions on their behalf.

Mr. Jim Baumgartner: The same is true for us, with the addition of MasterCard.

[Translation]

Mr. Jean-Yves Laforest: You charge fees directly to merchants. So, you act as intermediaries between retailers and card issuers. You charge fees to retailers and those fees do not come from MasterCard, Visa or the financial institutions? On what basis are they set?

[English]

Mr. Jeff van Duynhoven: In my opening remarks, I noted that interchange comprises the vast majority of the fees that we charge. So we have those costs, and I think Jim mentioned assessment fees that the card brands charge as well, so those are two inputs that we have. And then we have our own direct costs. We then have to determine how the merchant is processing cards, the type of cards they take, etc., and then we can determine a price to charge to that merchant, obviously being aware of what our competitors are charging in the market as well.

Mr. Jim Baumgartner: The fees are negotiated individually with each merchant, but the vast majority of the fee would be the merchant discount rate, the fee that we charge to the merchant. From a cost perspective, the vast majority would be interchange, and then assessments, and then our operating infrastructure as well.

[Translation]

Mr. Jean-Yves Laforest: The representatives of Visa and MasterCard all stated that they do not charge any interchange fees. Is that true?

[English]

Mr. Jim Baumgartner: That's exactly the case. Their fee base for their shareholders is generated from service or assessment fees, and that's included in our cost. So they will bill us quarterly, based on our overall volume, and then we'll remit money to both Visa and MasterCard as well as Interac for their fees.

And the card issuers do the same thing. So if you have a card issued by Desjardins, for example, all of your volume is added up, and Desjardins will pay issuing fees for those as well.

• (1605)

[Translation]

Mr. Jean-Yves Laforest: So, Visa charges fees to you and you charge them to retailers.

[English]

Mr. Jim Baumgartner: That is the case. In some cases we'll end up absorbing them. It's a negotiation with the merchant, depending on what the market will bear and what competition will bear. But yes, that's exactly right.

[Translation]

Mr. Jean-Yves Laforest: Only in some cases, you say?

[English]

Mr. Jim Baumgartner: Yes. Overall, as the interchange levels and the assessment levels have gone up.... And actually, as I looked at our last audited numbers through 2008, the interchange had gone up at a little over 2% a year, I think, in terms of their rate. And then our merchant fees had gone up about 1% a year.

[Translation]

Mr. Jean-Yves Laforest: What percentage of those fees from by Visa and MasterCard is charged to you? What proportion is transferred to retailers? You must have an idea. You stated that it is on a case-by-case basis and that it is based on negotiations but you must know the overall percentage. Are you charging the retailers 75% or 80%? I am sure that you have some idea of the amount.

[English]

Mr. Jim Baumgartner: Sure. In the case of the fee increases, what percentage has been passed on? It varies by merchant, but I would say with the larger merchants, typically they tend to be priced at whatever interchange is plus so many cents per transaction. That tends to be how most of them are priced. Smaller merchants tend to have either a blended rate or a couple of rates. So certainly with—

[Translation]

Mr. Jean-Yves Laforest: To be clear, here is the point of my question. Overall, you must surely be able to tell us what is the percentage of the fees charged to you by Visa and MasterCard that is transferred to the retailers? Is it half? Is it 25%, 75%?

[English]

Mr. Jim Baumgartner: Since 2001, with the changes, about half the fees have been passed on to the merchants.

[Translation]

Mr. Jean-Yves Laforest: So, it is about half.

I have another question about premium cards. I would like you to provide me with a clear answer, Mr. Van Duynhoven.

Who pays for the premiums? Is it the acquirers, the consumers, the merchants, the issuers or the company giving the premiums? I would be surprised if it were the company giving the premiums because nothing is free. Who pays for that, at the end of the day?

[English]

Mr. Jeff van Duynhoven: I can answer that.

In our case, Visa charges the acquirer the extra 20 basis points for the Infinite card. So I get charged all of that for every Infinite card transaction that is processed. As Jim has said, we then have to negotiate with our merchants. So we collect that premium charge from most merchants; some have contracts that don't enable me to pass on that charge, so I am absorbing that cost. I don't get anything extra but I still have to pay Visa that cost.

The Co-Chair (Hon. Michael Chong): Thank you, Mr. van Duynhoven.

[Translation]

Thank you, Mr. Laforest.

[English]

Now we're going to go to the member for Mississauga—Erindale, Mr. Dechert.

Mr. Bob Dechert (Mississauga—Erindale, CPC): Thank you, Mr. Chair.

Ladies and gentlemen, thanks for your presentations.

We've heard from some of the merchant associations that some of the merchant agreements they enter into with Moneris, TD, and others restrict them from disclosing the fees they are paying for their services. Is that true of any of the agreements that either Moneris or, say, TD Merchant Services has with merchants?

Mr. Jeff van Duynhoven: Nothing in our agreement prohibits them from disclosing what they pay.

Mr. Bob Dechert: Okay. Is that the same for TD?

Ms. Fern Glowinsky: Yes. From a Moneris perspective, we do have confidentiality provisions in our terms and conditions, and those relate to the terms in our contract and also with respect to pricing.

• (1610)

Mr. Bob Dechert: What is the purpose of that restriction on disclosure?

Ms. Fern Glowinsky: The purpose of that is to ensure, from a competitive standpoint, that our merchants are negotiating with us. I guess to the extent that the information is no longer confidential and over the course of time it becomes public, it wouldn't be continuously subject to that provision. From a marketing and competitive standpoint, our interest is in ensuring that our merchants are negotiating in good faith with us with regard to price.

Mr. Bob Dechert: Do you think the consumer has a right to know what the fee is that's being charged on the cost of the transaction?

Ms. Fern Glowinsky: Our price is different from the interchange rate, if that's what you're referring to.

Mr. Bob Dechert: I understand. There seems to be a major concern that consumers don't know the costs of using a credit card, and so I wonder what the damage to your business might be, if any, if disclosure of those fees were required.

Ms. Fern Glowinsky: I take your point, and I think the reality is that with the now-public information regarding interchange rates, consumers are increasingly aware of the cost. As we've said, the biggest component of our price is interchange, and that information is now public, so it's perhaps more of a dated provision, in fairness, with respect to our agreement.

Mr. Jim Baumgartner: I'd say it hasn't come up with merchants. They haven't asked us to be able to discuss it, to my knowledge, but it is something, certainly, that I don't know is still necessary in the agreements. It's something this whole process has taught us. We can do a little bit of self-reflection and we can improve in certain ways, and I think that's a good example of a way in which maybe we can improve.

Mr. Bob Dechert: Okay, I think that might be helpful.

Do your merchant agreements restrict merchants from advertising a cash purchase price on their goods and services?

Mr. Jim Baumgartner: No, they don't.

Mr. Bob Dechert: Okay, in none of your cases.

Do you collect higher fees for processing Infinite or premium credit cards?

Mr. Jim Baumgartner: Yes, we do in some situations and in some situations we don't. It depends on the actual agreement with a specific merchant. Each merchant negotiates individually with us.

Mr. Bob Dechert: Is there a higher cost for processing the Infinite or premium card versus another card?

Mr. Jim Baumgartner: The interchange is definitely much higher.

Mr. Bob Dechert: [Inaudible—Editor]...technology that you use?

Mr. Jim Baumgartner: Yes, there was. There's a substantial system investment, from our perspective, to be able to process the more complex cards, so definitely.

Mr. Bob Dechert: What you're talking about are the chip cards, is that right?

Mr. Jim Baumgartner: The chip as well as the more complex interchange structure, the premium cards.

Mr. Bob Dechert: I'm still not understanding that. What is it about the Infinite credit card that costs you more to process the transaction?

Mr. Jim Baumgartner: The change in interchange from what was a very simple structure in 2001 to now, as Jeff mentioned, 21 or so Visa rates and probably an equal number of MasterCard rates, which required us to have a major system build to be able to handle those transactions.

Mr. Bob Dechert: It has to identify what kind of card it is.

Is there any way that you could build into your system a point-of-purchase display that would then alert the merchant to the fact that it's a premium card on which a higher rate is being charged?

Mr. Jim Baumgartner: It's certainly technically possible. I think some of our merchants may have an issue with that, particularly those who deal with speed at the point of sale. Any quick-service restaurant, for example, would want to keep the customers moving and not slow them down to examine each of the types of cards. But it is technically possible, yes.

Mr. Bob Dechert: I wonder if each of you could let us know your views on the new credit card disclosure rules that were announced by the Minister of Finance last week.

Mr. Jeff van Duynhoven: I think they were really aimed at consumers or cardholders, so it doesn't impact our business at all because there is really no impact to merchants.

Mr. Bob Dechert: Do you think these would be helpful to consumers and merchants generally, the disclosure rules that were announced?

Mr. Jeff van Duynhoven: Again, I don't think there would be an impact directly to a merchant customer. As I said in my opening statement, we believe in transparency, so for consumers, more transparency is always a good thing.

Mr. Bob Dechert: So from that perspective it would be an improvement.

Do you agree, Mr. Baumgartner?

Mr. Jim Baumgartner: Yes, I think from a consumer perspective, as a cardholder, I think they were well thought through. They were good from a cardholder perspective. And as Jeff said, disclosure is something we can all do better at.

So from that perspective, I would say yes. From a merchant's perspective, I would say there is less impact, but to the consumer, definitely.

•(1615)

Mr. Bob Dechert: Thank you.

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. Dechert.

Mr. Thibeault.

Mr. Glenn Thibeault (Sudbury, NDP): Thank you, Mr. Chair.

Thank you to the witnesses for coming again today.

I want to jump right to a few questions that my Liberal colleague was asking a few minutes ago, related to priority routing. I would like to get some clarification on that.

Is that a system that is implemented now, or is that a system that is planned for the future?

Mr. Jeff van Duynhoven: In terms of what TD does today, we do not do any priority routing, because we don't support MasterCard Maestro and Visa debit is not yet in the market. So as of today we don't do anything. As I did say earlier, we will support Visa debit, and the choice that Visa has made is to make that a consumer choice at the point of sale.

So if a merchant has elected to accept Visa debit...and this is important to mention. The merchant has to elect to accept Visa debit. So they choose to accept both Interac and Visa debit. If that is the case, and if a card is presented that has both the Interac and the Visa debit application on it, then and only in that exact circumstance will the point-of-sale terminal provide a choice to the consumer. The consumer can then elect to process that transaction as a Visa debit transaction or as an Interac transaction.

Mr. Glenn Thibeault: I'd like to come back to Moneris to answer that question, but in relation to that, we had Visa Canada here last week, and I believe they stated that if you have a Visa credit card you're going to have to take all Visa credit cards or debit cards. Is this going to be true for a merchant if they choose not to take the debit card?

Mr. Jeff van Duynhoven: Visa has elected to enable merchants to elect to accept Visa debit separate from credit. It's commonly referred to as the honour-all-cards rule that Visa has, and they do have that rule. So if you accept a Visa credit card, you have to accept all Visa credit cards. But they've made the choice to say that if you don't want to accept Visa debit and you just want to stay with Interac, that's okay. That's allowed.

Mr. Glenn Thibeault: Great.

So Moneris, I'll go back to my first question.

Mr. Jim Baumgartner: On the Visa side, it's exactly the same answer. We believe that method makes the most sense. We think the consumer should have a choice on how their transaction is treated. Our devices will prompt for it, for the merchants that elect to accept it. We're very pleased that Visa has not elected to enforce the honour-all-cards rule. We think that can be problematic, particularly with respect to debit versus credit.

Does that answer the Visa question?

Mr. Glenn Thibeault: Sure.

Mr. Jim Baumgartner: On the MasterCard side, MasterCard has chosen a slightly different path. They've brought the cost down of processing the transaction. Their assessment fees are now actually lower than Interac's, which is positive for the merchants, but their method is a bit different in that the banks are instructing us where to send the cards, as opposed to the individual cardholder, so the banks are making the decision.

From a merchant perspective, at this point it actually matters less. In fact, in some cases, if they hold true to keeping the assessment fee at a competitive advantage versus Interac, it'll actually be a good thing for the merchants to the extent that they're billed on an assessment fee basis.

•(1620)

Mr. Glenn Thibeault: I'd like to get clarification on this. If this happens, I am the consumer, I have my card, I'd swipe it; I now have the remote—or whatever the technical terms is—in my hand. I have a choice of credit, debit, or other. “Other” would be Interac, for example, because you still have to offer that as a merchant as well, is that correct?

Now, if I choose “debit”, that's going to be priority routing. Is priority routing going to be higher if I choose “debit” rather than pushing “other”? I don't know what “other” is. Will merchants then have to inform people where they should be choosing to push, to make sure the costs are lower?

Mr. Jim Baumgartner: In the case of Visa, it's a prompt. It's either Interac or Visa debit. As for the card you would use, if you have a client card where you get cash out of your debit card today, you would be prompted with Visa for either Visa debit or Interac. You can choose either one. It will still go into your bank account.

With MasterCard, there will not be a prompt the way it's currently envisioned. This has not been rolled out yet. This is still being built. The way it's envisioned, the transaction would not be slowed down with the prompt. It would go right through Maestro if your issuing bank issues Maestro and they instructed us to route those transactions through Maestro.

Ms. Fern Glowinsky: I have a point of clarity that might help. The instructions will actually be on the card. When you get your debit card, the card will already have been predetermined in terms of a debit card from a MasterCard bank that's also offering Maestro. The card will be predetermined in terms of how to route the transaction.

Mr. Glenn Thibeault: I appreciate the fact that it's going to be on there, but we've been hearing about the issues with small print for the last few months. Once again, we're getting another document with small print. We want to make sure that everyone is informed, so if there is any way we can change it from the small print to make sure consumers know, that's what we want to do. The more we talk to consumers about interchange fees and all the little fees that the merchants are paying, they're starting to understand the importance of not dinging merchants with their big premium cards along those lines, so I think that's an important piece.

One of the things I haven't heard yet is, will the priority routing fees be higher than average regular Interac fees, if I am choosing debit on Visa or MasterCard?

Mr. Jim Baumgartner: I'll start with that.

With Visa, as it's currently envisioned, they will be higher, because Visa has set their interchange level at a level that, in our opinion, is too high. They believe there's value brought, and there is value brought in both scenarios. For example, if you buy something online and you dispute that it was you, with Interac you're more of an unsecured creditor. Visa and MasterCard have a policy that will protect you, so there is definitely value there.

In Visa's case it will be more expensive, upwards of maybe three times more expensive on average. It'll vary by merchant. With MasterCard it actually wouldn't be more expensive, because they've committed, so far, to holding consistent with or lower than Interac.

Mr. Glenn Thibeault: We've heard, I believe, from 250,000 members of the RCC, the 2.4 million from CFIB, and they're all talking about the concerns they have with interchange fees. I think instead of adding higher fees, we need to start looking at what we can do to be more transparent so we can get everyone on the same playing field.

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. Thibeault.

Mr. Rota.

Mr. Anthony Rota (Nipissing—Timiskaming, Lib.): Thank you, Mr. Chair.

Thank you for being here today.

I was just going through this, listening to the priority routing. I just want to clarify if the priority routing comes up on the terminal. Does it show up anywhere? I know you've answered this question earlier, but I'd like some clarification. I'm not 100% clear on how this works.

I show up with my card and it gets swiped. Now with priority routing, from what I understand of Visa or MasterCard, depending on whose program gets that priority, is that priority a benefit to the merchant? How does it work, and who gets the benefit by that priority being there?

Mr. Jeff van Duynhoven: I can start.

I wouldn't characterize Visa debit as priority routing, because the consumer does have the choice. What will happen is that on the point-of-sale dialogue.... Today, if you use your debit card, the terminal dialogue will ask you after you've swiped your card—and in this case, it would have to be a chip card, so it would only be applied to a chip transaction—if you want to pay by Visa debit or Interac. You will select Interac by pushing a button on there, just as you do today. The dollar amount of the transaction will come up, and you will confirm that and enter your PIN, etc., and the transaction will be processed. So you have, as a consumer, selected Visa debit.

As Jim has said, MasterCard has taken a different approach and has implemented priority routing. So the bank has issued a card with Interac and Maestro on it, and if it comes to an intersect, a merchant who actually accepts the Maestro MasterCard transaction.... Again, that's important to distinguish: the merchant has to be enabled for Maestro. If the merchant is enabled for Maestro, there is no terminal dialogue in that case, because the bank and the merchant have essentially agreed. The bank has issued a card to a consumer that will be processed by Maestro, and the merchant has agreed to accept Maestro, so in that case it will get priority routed to Maestro versus Interac.

Mr. Anthony Rota: So there's no pre-arranged agreement that automatically defaults to one or the other. It depends on the card, not on the merchant agreement with the bank?

•(1625)

Mr. Jeff van Duynhoven: It depends on the merchant agreement with the bank, because the merchant has to agree to accept Maestro and/or Visa debit. So unless that happens, the transaction would not be processed through either of those two means.

Mr. Anthony Rota: Okay. I'd like to come to back something else, and then I'll come back to the priority routing.

But one of the areas that really concerned me was the shifting of liability. One of the features as a merchant is that when you are taking in money through plastic—through a credit card or a debit card—you don't have to worry about the liability. You are basically selling your receivables and taking the money in, and there are no more worries.

With the shifting of the liability to the merchants, I'm concerned about two things. One, there is the cost of all of a sudden having to self-insure, because not having to do that was one of the big features. But the other concern I've heard is that with the new technology, with the chips, I understand there are some changes coming up to the terminals themselves. For large merchants that's an issue; it's a cost, but they can absorb it. But for smaller merchants, who will be absorbing the cost of this shift? Do they have an option not to shift over to the new technology, and what would be the consequences if they didn't shift?

Mr. Jeff van Duynhoven: That's an excellent question, and Jim can certainly add to this.

Getting ready for the chips has been a very expensive proposition for all acquirers. We've spent tens of millions of dollars preparing our systems, because our systems need to change, and the industry has probably spent hundreds of millions of dollars buying new point-of-sale devices. I know that for TD Merchant Services, it has been north of \$50 million over the last several years that we have spent from our capital to purchase new point-of-sale devices, which get deployed by us because the average merchant ends up having a rental agreement with us as part of the services. So as part of the monthly fee they pay for POS rental and servicing of that device, we've built in redundancy. So I will send a service technician out to that merchant site, where we'll deploy a new chip-capable terminal for them, at typically the exact same or lower cost than the old terminal that's out there. So we've enabled those merchants.

Mr. Anthony Rota: So you're telling me there's no increase in cost to the merchant?

Mr. Jeff van Duynhoven: For the vast majority of merchants, no, there has been no increased cost.

Mr. Anthony Rota: And for smaller merchants as well?

Mr. Jeff van Duynhoven: That's correct, yes.

Mr. Anthony Rota: Okay. I'll let you continue.

Mr. Jeff van Duynhoven: The risk to the merchant with this liability shift that will occur in October 2010 only exists if there is not a chip-capable device processing that transaction.

Our goal is to enable all of our merchants with chip-capable devices before October 2010. And we're well over 60% of the way there, so we've converted already 60% of our merchants to chip-capable devices. Again, as Jim said at the outset, if the merchant isn't capable of taking that risk because they don't have the funds on hand or if they were to go bankrupt, etc., that liability falls to the acquirer. The acquirers are not a fan of this new regulation either, but it has caused us considerable expense to go and retrofit our customer base.

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. van Duynhoven. Thank you very much, Mr. Rota.

Mr. Brown.

Mr. Gord Brown (Leeds—Grenville, CPC): Thank you very much, Mr. Chairman, and I want to thank our witnesses for being here today.

My background is in the lodging and food service industry, so I'm quite familiar with what you do, from a merchant standpoint. It's a really good thing that you're here, because we've been hearing much from the Canadian Federation of Independent Business, so it's great that you're here to explain exactly how you operate.

Mr. Rota had some good questions and I want to follow up on those. I want you to explain a little bit more about this liability shift and what that is actually going to mean for a merchant. Could you possibly use an example, say in the lodging industry, that some of us might understand? I know that we've taken many cards over the years and I don't think that all cards are going to be chip-enabled by 2010. Is that going to mean that the merchant is going to take on liability that they currently don't have right now?

The floor is open on this.

Mr. Jim Baumgartner: If you owned a hotel, for example, and it didn't have a chip-enabled device, and if you were renting from either me or Jeff or the other dozen or so competitors in the marketplace, we would, by October 2010, send out a technician and we would replace the device with a chip-enabled device. Once that chip-enabled device is in, then from the hotel owner's perspective, there is no increased liability because we have a device in there.

In fact, from a hotel perspective, you'll actually be better off because our data, so far at least.... The market hasn't been flooded with chip cards yet, but to the extent that we've had chip card transactions, our data show that the numbers of disputes—if you had disputes before at the hotel such as, "It wasn't me staying there", etc.—have come way down.

From our perspective, from Moneris' perspective, we actually do support the introduction of the chip in Canada. We think it's a more secure way of paying. We don't support the liability shift happening as quickly as it has. We think it's a bit of a burden on the merchants that is not currently needed.

Let's say you owned your own device, as a hotel. Let's say you purchased your device and you had just invested in it and it wasn't chip-capable. If someone showed up at your hotel and disputed the transaction and said, "That wasn't me", and you didn't have a chip-capable device, then you'd lose that dispute. So there is increased liability in the case where you do not have a chip-enabled device. But as Jeff pointed out, the vast majority of the devices that'll be deployed will be chip-enabled by October 2010.

• (1630)

Mr. Gord Brown: But let me go back just one second on that. If you go to a hotel, generally what they do is take an imprint of your card and you sign the registration card. So if there is a dispute, usually there is that sort of backup. Now, of course, with the chip and people putting in their PINs, that's going to be doubled. But is that going to mean that on cards that are not chip-enabled, this other backup in terms of the liability of someone saying it wasn't them staying...are those hard validators still going to be accepted?

Mr. Jeff van Duynhoven: That's an excellent question. That's exactly the point I was going to make, because I think in your first question you had asked, if the card is not a chip card, does the merchant have that liability? And the answer is no, it's no different from what it is today. So it's only if a chip card is presented at a non-chip-capable point-of-sale device. If the bank or credit union or other issuer has not provided you, as a consumer, with a chip card, then the liability is exactly the same and you would do exactly as you've said today. You would use your imprinter to prove that the card was in fact present for that transaction if there was ever a dispute.

Mr. Gord Brown: I don't know how much time I have, but I do have one question that I'm sure many merchants will be asking as Visa debit and Mastercard debit or Maestro roll out. Why would a merchant not want to accept those debit products?

Mr. Jeff van Duynhoven: In the case of Visa debit, I think they would like to accept them for contactless capabilities, so the tap and go capability, or for e-commerce or other card-not-present transactions. Those are new opportunities for them to use that particular card. The reason they wouldn't want to accept it is that Interac works today at the point of sale for debit. As I said in my opening remarks and Jim has mentioned, there is interchange attached to Visa debit. So at the point of sale, at this point in time, just on the pure cost equation it would be questionable whether they would want to take that card. Again, they'll have the choice to not accept Visa debit at the point of sale.

Mr. Gord Brown: A Visa debit transaction would be at a set fee or at a percentage fee?

Mr. Jeff van Duynhoven: It depends on the acquirer. Acquirers determine the price. Today there is zero interchange on Interac transactions, but there still is a cost obviously to the merchants for us to process. In the case of Visa debit, the electronic interchange rates—so when the card is there—is five cents plus 25 basis points. So that is an increased cost for the merchant. But the acquirer still needs to charge for all of its other costs, so it will be north of that particular transaction amount.

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. van Duynhoven.

Thank you very much, Mr. Brown.

[Translation]

It is now Mr. Vincent's turn.

Mr. Robert Vincent (Shefford, BQ): Thank you, Mr. Chairman.

Thank you to the witnesses. I have a few questions.

Earlier, you stated that Visa and MasterCard do not get anything from the interchange fees. Did I understand correctly? If those companies do not receive anything from the acquirers or from the banks, can you explain why they are the ones setting the interchange fees?

• (1635)

[English]

Mr. Jim Baumgartner: Visa and MasterCard do not make money from interchange. Their revenue model is driven off assessment fees that are charged to merchant processors like us as well as assessment fees that are charged to the issuers. So it's in their best interests to try

to maximize the flow-through of volume in the system. The more charge volume that goes through the system, the more we end up paying in assessment fees, the more the issuers end up paying in assessment fees, and that's in their best interest. So what they have to do is try to balance the interchange rate and set the interchange rate in a way that maximizes participation in the system. In that respect, they'll be able to get as much volume as possible.

So things like the contactless debit, for example, as Jeff pointed out, would be innovations that would bring more volume into the system, presumably generate more assessment fees, and make their shareholders happy.

[Translation]

Mr. Robert Vincent: You stated earlier that you were not involved at all in changing the interchange fees of the credit cards. Since Visa and MasterCard do not get any money from that, how come you are not involved in setting those fees, even when you talk about volume? If the interchange fee was set at 1%, the volume would be the same as if it were set at 2%. You collect money on all the transactions and you claim that the interchange fees are too high.

Why are you not putting the question to Visa and why do you not ask them to lower the interchange fee? Is there a particular reason?

[English]

Mr. Jim Baumgartner: In the case of debit, we actually did have some success with MasterCard. They had a model similar to what Jeff had described with Visa. In that case we were able, with others I'm sure, to convince them that a more competitive model was appropriate given their current situation. They did listen. I'll give them credit for that.

In the case of credit, I think the challenge, at least with their premium cards, has been trying to compete against American Express, which has historically had a higher-end customer, those who charge more. The worst thing that could happen in the system today would be if they weren't able to compete against American Express for those higher-end customers, if the interchange rate was too low and banks decided to start issuing American Express cards, because those are much more expensive than Visa and MasterCard. Even the premium Visa and MasterCards are less expensive than Amex is today.

[Translation]

Mr. Robert Vincent: I have a final question.

It relates to smart cards. You said that starting in October 2010 the retailers will be liable if payments are not processed correctly. If that is the case, are you going to provide them with the equipment needed to read those cards free of charge or will they have to pay something to replace their equipment?

Also, do you believe that interchange fees could be reduced when the liability for chip cards is shifted to the retailers?

[English]

Mr. Jim Baumgartner: With respect to your first question, in terms of fees, we are not planning on any fee increases as a result of deploying the new terminals. We now have probably about 140,000 or so chip-enabled devices at our various merchants. We're working on replenishing them by 2010, to make sure those who need them will have them.

Our average terminal rental rate has come down over the last few years. So even though the equipment has gotten a little more expensive, the actual rate has come down so the merchants won't bear it. There's one exception, and that is the merchants who own their own devices. They tend to be the really large merchants. They'll have to upgrade and purchase new equipment to be able to handle the transactions. They'll have to do work at their host. This is a very expensive proposition for, generally, the major merchants, because a lot of them will own their own devices.

In the case of the smaller merchants, we tend to own them, and we tend to rent them.

[Translation]

The Co-Chair (Hon. Michael Chong): Thank you.

Mr. Carrier, you have one minute.

Mr. Robert Carrier (Alfred-Pellan, BQ): Thank you.

Good afternoon, lady and gentleman. I would like to come back to the issue of premium cards. Who bears the additional cost of interchange in the case of premium cards?

You are aware that Canadian and Quebec coalitions of retailers have spoken against those cards because there will be additional costs to them.

Mr. Van Duynhoven stated that, sometimes, you absorb the additional costs of interchange for chip cards.

Did I understand correctly? Is that the case?

• (1640)

[English]

Mr. Jim Baumgartner: It varies by merchant. But in some cases, if we have a fixed rate for the merchant, we end up eating the difference.

[Translation]

Mr. Robert Carrier: Since you are not in business to lose money, I suppose that this additional cost will in the end be added one way or another to all the operational costs you charge to the retailers.

Since I do not have too much time, I want to know a few things. You know that retailers' coalitions have also recommended the Australian system for setting the interchange fees.

What do you think of that suggestion?

[English]

Mr. Jim Baumgartner: In general, I suppose, my view is that government-imposed price controls on businesses tend to not work. It's more of a commercial dispute.

One of the issues that I'd have with it, having read a bunch of the studies, is that there are pros and cons. I don't know if you've had a chance to read some of the studies, but there are a lot of cons and there are some pros to what they did, at least according to the studies that I happened to read. One thing that definitely happened was, because they didn't include American Express in that endeavour, it ended up benefiting them unfairly, I would say from my perspective. And also, I think to the extent that you did that, in this particular instance—and we had banks that migrated their issuing portfolios to American Express—the merchants would be in a much worse situation because the average rate for American Express is much higher than it is for MasterCard and Visa, including the premium cards.

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. Baumgartner.

[Translation]

Thank you, Mr. Carrier.

[English]

Now we have the venerable chair of our Standing Committee on Finance, Mr. Rajotte.

The Co-Chair (Mr. James Rajotte): Thank you very much, Mr. Chairman.

Thank you all for coming in today.

I want to address my questions to you, Mr. van Duynhoven, because you've provided some documentation that I think is helpful here. What I really want to do is to drill down to try to understand all of the fees that are being charged to merchants.

First of all, you have the Visa corporate, commercial, and business card transaction fee, which, if I'm reading this correctly, increased, according to this letter of February 2008. You have a Visa Infinite card transaction fee, which is a new fee. Then you have a Visa assessment fee, which seems to be a new fee as well. And then you have the merchant discount rate, which, interestingly, actually decreases, according to the documentation here.

The merchant discount rate includes, according to the information we have, the interchange fee plus other costs. What proportion of the merchant discount rate is the interchange fee?

Mr. Jeff van Duynhoven: Again, it would depend on individual merchants. It depends on how the merchant does the processing and the risk involved with that transaction—if, for example, it's an airline or a tour company or a furniture store. Any organization that has delayed delivery has increased risk for the acquirer. So it's difficult to say in total what it is, but on average—

The Co-Chair (Mr. James Rajotte): Seventy-five per cent?

Mr. Jeff van Duynhoven: Yes, at least 75%, probably, of our cost is the interchange cost.

The Co-Chair (Mr. James Rajotte): Seventy-five per cent of the merchant discount rate is the interchange fee. And these three fees you have here, which you've outlined, are those all included within the merchant discount rate?

Mr. Jeff van Duynhoven: No, it happened when the interchange rates changed; now they all are driven and there are differential interchange rates attached for each type of card. So a commercial card has a unique set of fees or interchange rates attached to it, as does an Infinite card, as does a regular consumer card. So what we've done is we've tried to articulate that and manage that so the merchant understands that my costs have gone up, for example, 20 basis points for an Infinite card and 36 basis points for a commercial card. We've tried to reflect that on the statement and pass that increased cost on in the example we've shown.

The Co-Chair (Mr. James Rajotte): And why is the merchant discount rate decreasing in this example?

Mr. Jeff van Duynhoven: Again, depending on how the merchant was processed before, we did not pass through the commercial card transactions. As I said in my opening statement, in some cases we blended the rate. As an example, we would have said the merchant discount rate was 2%. We may have now moved to 1.8% plus 20 basis points for Infinite or plus 36 basis points for commercial. So we've tried to unbundle the pieces to better reflect the new structure Visa has implemented.

• (1645)

The Co-Chair (Mr. James Rajotte): So if I'm a merchant and I'm paying this merchant discount rate, my merchant discount rate may have in fact gone down. My interchange fee will vary because it has gone from two to 21 possible rates. But with these three fees, if somebody does walk in with an Infinite card, in fact they'll have an increase in the first type and the introduction of two fees that were not there previously, on top of the merchant discount rate? Am I correct in saying that?

Mr. Jeff van Duynhoven: Yes, and there could be more fees. There could be standard fees charged, again, for the way the transaction is processed. So there could be different fees that we pay. The merchant can no longer say, "I pay 1.8% as a merchant discount rate and that's my all-in cost."

As I tried to articulate in the opening remarks, that's the way it used to be. It was much easier for merchants and it was much easier for acquirers to go and levy those costs. Now with the complexity, we've had to spend lots of money to re-do our systems, and the industry has typically tried to break out those transactions.

The Co-Chair (Mr. James Rajotte): Has this complexity been imposed on you by the credit card companies?

Mr. Jeff van Duynhoven: Yes. They change the interchange rates. They don't consult with us to see what we think; they change those.

The Co-Chair (Mr. James Rajotte): You, as companies, preferred the much simpler system that was in effect before?

Mr. Jeff van Duynhoven: Certainly I would have preferred to stay there, yes, because we've had to spend considerable sums of money, and clearly, merchants are upset with the increased costs associated with it.

Mr. Jim Baumgartner: If I could just add this, there are actually some good instances where varying interchange makes sense, in my experience. I don't know if you have government travel cards when you travel. You don't have government travel cards? Okay, I used to work on the issuing side in that particular space. It used to be that

Diners Club and American Express had a lock on the market, and when Visa and MasterCard introduced different interchange rates for those particular products they allowed issuers to compete against Amex and Diners Club in that particular space.

Then in some cases, not here yet in Canada, although I would argue it would be a good thing, when merchants pass additional data along, as with purchasing cards—I think you have a purchasing card program—that additional data helps companies streamline their costs. There are arguments for tiering interchange to incent merchants to do that.

So it's not as though a more complex interchange system is inherently bad, although overall it has made our lives a lot more complex.

The Co-Chair (Mr. James Rajotte): Unfortunately, my time is up, but I appreciate this.

Any more information you have explaining to members of this committee all the fees that are new or increased or that apply to merchants would be helpful. We have a fairly good explanation of a four-party model, but still, any more information you have on that would be helpful. We'd appreciate it.

The Co-Chair (Hon. Michael Chong): Thank you, Mr. Rajotte.

Mr. Thibeault.

Mr. Glenn Thibeault: Thank you, Mr. Chair.

Just going back to that one question I wanted to get in, it was relating to priority routing and the new terminals. Will merchants have to get involved with that? Do they have the option of staying out of priority routing and just keeping the current system, or ultimately will that be the new system that's phased in?

Mr. Jim Baumgartner: If merchants do not want to accept Maestro, we certainly would never force them to do that. We will turn it on.

Mr. Glenn Thibeault: What about with Visa?

Mr. Jim Baumgartner: Yes, with Visa there will be a prompt at the point of sale. Also, the merchants will have to elect whether they want Visa debit as well.

Mr. Glenn Thibeault: Thank you.

Mr. Jim Baumgartner: That would be as long as Visa sticks to the non-enforcement of the honour-all-cards rule, which is very important in that answer.

Mr. Glenn Thibeault: Thank you.

I want to jump a little bit to the question of liability and some of the fees we've been hearing about. I was interested to notice, in following the collapse—I believe it was in April—of Conquest Vacations, that they talked about unrealistic and unreasonable demands by credit card processing companies being one of the determining factors. There was also a piece in the *Globe and Mail* about credit card processors making them hold on to \$900 million. I think there was some resolution of that. I'm not sure.

Could you talk to that point of having to have this cash in reserve and then companies coming out saying these things?

Mr. Jim Baumgartner: I'd love to, and thank you for raising the question.

I'm going to distinguish between an airline and a travel agent. There are government agencies involved in the tour operator business. In the case of the tour operators, TICO, if you're familiar with it—and there's a fund in Quebec as well—protects the travellers. They will require the tour operators to place on deposit funds for future trips. If you buy a trip to Cancun in June, for example, and it's a thousand dollars, and let's say you buy it from a major tour operator, that tour operator will have to place the money in a trust fund. However, if that tour operator were to fail, and let's say you were the merchant processor, you would dispute the transaction with your card issuer. We, as the merchant processor, would end up absorbing that charge if the tour operator was out of business. So we require, in the case of the more challenged tour operators, deposits as well.

So the tour operators are being doubly penalized, because the funds are holding money and ultimately, if it's charged on a credit card, the merchant processors get charged. That's a real problem for the industry. If there's anything anyone can do to help that particular industry out, they really need the help. I think Conquest was, in part, a victim of that particular situation.

In the case of the airlines, there is no such regime. We process for both. In the case of the airlines, we have a great big credit department that would look at the risk. If you own an airline and your airline is profitable and has plenty of cash and so on, we may not require a deposit. If you are more challenged or are going through some tougher times, we may require a deposit to protect against the risks I alluded to earlier.

● (1650)

Mr. Brian Crozier: Can I add something about Conquest?

Have you ever noticed that you can't buy an airline ticket in this country unless you have a credit card? If you don't have a credit card, you can't buy an airline ticket. It's the only country in the world like this.

If you really want to help that industry, what you need to do is help people use their money to make that payment online. Air Canada needs the help of UseMyBank so they can accept payments from their customers in real time at a rate that is going to be competitive with Visa and MasterCard. Instead of so many regulations, we could have competition help drive those prices down.

The technology has been here for 10 years, and we're the only country that is not using it. We have Visa and MasterCard that want to have the entire market to themselves. We have online banking, and we have customers who want to receive those payments. There's really nothing in the way of making it happen.

If you buy a \$5,000 trip, you don't have to pay 3% to Visa to get that job done. It can be done for a lot less than \$150 on that transaction. That's what we're talking about.

At UseMyBank, we're only in the online world. When you talk about point of sale, it's a place we're not at. But in the online world, I think Canada needs to have some more ability for customers, if they

want to make cash payments, to make them. If they decide they want to use Visa, they can use Visa. But we need to have more choices, I would say. Conquest Vacations, I think, could still be in business if they'd had that edge, that competitive edge, to offer their customers the ability to pick a debit payment.

Thirty to forty per cent of people don't have Visa or MasterCard. If you don't have a credit card, you can't shop online. It doesn't seem fair. It seems that you need to have two systems to reflect the same values as you have in the physical world, where you can shop with your cash, your debit, and your credit. When you go on the Internet, you're stuck with credit cards only.

I think Canada needs to have some kind of regulation or something in place to allow merchants to accept cash payments from customers who decide that they want to use their online banks. It makes sense.

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. Crozier, that was helpful.

Thank you very much, Mr. Thibeault.

Mr. Lake.

Mr. Mike Lake (Edmonton—Mill Woods—Beaumont, CPC): I want to direct my questions to Mr. van Duynhoven.

I'll go back to the letter, and to the statement that you provided us as well. I'm not sure that I'm any clearer, having been provided a sample statement, in terms of the flow of information. Maybe you can help me with this.

First of all to the letter, though, you mentioned that the letter is designed to kind of clarify situations for customers, but I notice that you use an example in your chart. You talk about the Visa corporate, commercial, and business card transaction fee and you use an example. With this fee change, a \$75 transaction processed by your business will cost about 9¢ more than the current calculation. I think you're probably using that example to show that it's not much of an increase. Then with the Visa Infinite card transaction fee, which is a new charge—50 basis points—there is no such example. I would note that on the same \$75 charge, it was easy to calculate using your number, and it looks like it would be about 37.5¢ more that they would pay.

Why would you not have an example there?

● (1655)

Mr. Jeff van Duynhoven: That's a great point, and several of our customers pointed that out to us as well. Essentially, that was a miss on our part.

Mr. Mike Lake: Only it seems that oftentimes the miss happens to be when the change is to the detriment of the customer.

Mr. Jeff van Duynhoven: As I said, we pride ourselves on transparency. When we look at what some of our competitors have done, we think we still are very transparent with that. We've clearly articulated...in this example it was 50 basis points extra, you're right. We've learned, as we've gone through some of this, that some customers don't understand what basis points mean. We didn't put a tangible example in that particular case.

Mr. Mike Lake: I think it illustrates the importance of the communication and some of the challenges here.

On the extra charge, I'm curious about the Visa Infinite transaction fee. Some people talked about 20 basis points or something, but in the letter it says 50 basis points. Is there an extra charge? Do TD Merchant Services make any extra money or charge extra for any of your clients when they use the Infinite card?

Mr. Jeff van Duynhoven: Yes, and in this particular example it was a 50 basis point charge. To answer your question directly, yes, some merchants pay more than the 20 basis point cost.

Mr. Mike Lake: TD Merchant Services is actually making more money now. It's not any more complicated for you to do that transaction, but you're charging a surcharge on top.

Mr. Jeff van Duynhoven: We're charging a surcharge on top because, as I said in my opening remarks, those changes cost millions of dollars for us to change our systems to be able to process these incremental cost transactions. We need to be able to recoup our cost. As any good business person would, we look at the cost and ask how we can do that and do it in a fair and transparent manner. That's what we've done here.

Mr. Mike Lake: It's largely an equipment cost.

Mr. Jeff van Duynhoven: Equipment and technology costs. It's less on the equipment side because it's not a point-of-sale device; it's more our own internal processing systems.

Mr. Mike Lake: Okay. Where I was actually going was to the point-of-sale devices.

I'll move to the other statement you have here. Perhaps we could walk quickly through who sets what and who gets what.

First of all, simply to clarify on the point-of-sale devices, I notice there's a rental charge of \$35. Is that per hand-held set-up?

Mr. Jeff van Duynhoven: This is again an illustrative statement. Customer fees will range depending upon the individual negotiation with that merchant and the type of equipment they have. Do they have a stand-alone point-of-sale device? Do they also want a PIN pad attached? In that case, I have to buy two component pieces. It really does depend on the individual client preferences of what they need and require to run their business.

Mr. Mike Lake: At the very top of the summary of fees, that goes to Visa, is that right?

Mr. Jeff van Duynhoven: No. That is what we have called the merchant discount rate. We are only a Visa acquirer, so we process the transactions for MasterCard but we don't bill for the MasterCard transactions. It's complicated, unlike Moneris who—

Mr. Mike Lake: This sample company would actually get a separate statement for MasterCard as well.

Mr. Jeff van Duynhoven: A statement for MasterCard, that's right. That's really the legacy out of the Competition Bureau previously not allowing duality in Canada. They've since lifted that restriction, last November, but currently this is a legacy of that. We process Interac and Visa transactions for our merchants directly.

Mr. Mike Lake: So the Visa discount fee is set by Visa.

Mr. Jeff van Duynhoven: No, that is our merchant discount rate. We've elected to pass those fees on. The Visa discount rate is set by

TD Merchant Services, and that's the charge we levy to the merchant for processing their Visa credit card transactions.

The Co-Chair (Hon. Michael Chong): Mr. McTeague.

Hon. Dan McTeague (Pickering—Scarborough East, Lib.): My thanks to the witnesses for being here.

I wanted to let everybody know the price of gas is dropping a penny tonight in some parts of the country.

Outside the country, there seems to be some concern about Visa and MasterCard attempting to get into the debit business. I think it behooves some of the members on the committee to find out whether there is any process by which debit clearing would take place outside of Canada. Is there a risk? I asked this question to Mr. Stanton, and he said no. But his answer was not clear. He guaranteed the clearing house for processing debit will not take place outside of Canada, which could bring forth concerns having to do with the USA PATRIOT Act and our own privacy laws.

Mr. van Duynhoven?

• (1700)

Mr. Jeff van Duynhoven: We process those transactions. Everything is processed in Canada. We don't send information outside Canada. However, we do send information to Visa, and Visa is a global company. In a technical session, we transmit information to Visa on our premises. We give it to a Visa server, and then they take it over their global network. As to where that transaction routes, I can't definitively say. I think the same would be the case for MasterCard.

Hon. Dan McTeague: So we can't be sure that it will find itself in the United States or under the jurisdiction of another country?

Mr. Jeff van Duynhoven: Credit cards are processed globally today. I can't be certain, no.

Hon. Dan McTeague: Mr. Baumgartner.

Mr. Jim Baumgartner: As to the way the electrons flow, in the case of Visa I think those servers would go either to McLean, Virginia, or Denver. In the case of MasterCard, I believe it goes either to St. Louis or Kansas City. That's something that we should confirm for you, or perhaps we could ask the card companies to diagram it out for us.

Hon. Dan McTeague: I think that brings in a whole level of interest that this committee will want to look a little closer at.

Mr. Baumgartner, in connection with the priority routing and the new point-of-sale machines, with the advent of chip cards and the probability of their being pervasive in the next few years, how likely is it that a merchant will be able to refuse to use the new priority routing machines? You said earlier that they have the option of not having them—for instance, Maestro. But given where we're going with these cards, is it not likely that saying no would also mean putting yourself out of business?

Mr. Jim Baumgartner: In the case of chip cards, they'll essentially replace the mag-stripe cards that we have today. It's the intention of Visa and MasterCard, as well as the Interac issuers, to gradually replace all of their cards with the chip technology. We have found that from a merchant perspective the chip technology is a positive thing. We found "It wasn't me" disputes to have gone down. Most countries in the world are moving towards chip. We have a sizable presence in the U.S. We're trying to encourage the U.S. to go to chip as well. Most countries, including most in Europe, are moving to chip. France went there a long time ago, and it's chip-and-PIN, which we believe ultimately is the most—

Hon. Dan McTeague: Mr. Baumgartner, using existing technology would not work. You could not use the same machines. I think you know what I'm getting at. Let's be honest, we're dealing with new machines required, and merchants will not be able to refuse. If they're not able to accept the new chip technology and the cards and fees that go with it, they'll be electing to go out of business.

Mr. Jim Baumgartner: That's not quite accurate, depending on the type of merchant. If you were a merchant who had very little dispute activity, a restaurant, for example, where almost no one disputes whether the meal was good, where the returns are very low, you may not need a chip device. Please keep in mind that the cards themselves will still have a magnetic stripe on the back. For example, when you go to the U.S. or anywhere else that doesn't take chip cards, and you want to buy something, you'll still have a magnetic stripe. The issuer will need that for you to be able to buy something, say, in the United States. We will still need to be able to process mag-stripe transactions, since we have U.S. customers coming to Canada and using the machines.

Hon. Dan McTeague: Mr. Baumgartner, I have a very simple question for you on a very complicated case. Someone has reported to me a problem they have with respect to fees they've been charged for non-qualified purchases. It would appear that the charges were placed on the wrong item on the bill, some for qualified, some for non-qualified. I'm wondering, given the example that's here, what this means for merchants as far as card acceptance is concerned, when they don't know how large the volume is of non-qualified cards. The concern by a number of these companies is that the line items in which something may be charged may not reflect the actual number or kind of client card they have, and they obviously have no right to refuse. How do they get around that conundrum, and do you have instances where you may be charging them the wrong line, in terms of the bill you're providing them?

• (1705)

Mr. Jim Baumgartner: We don't believe we do. We also have reporting that would delineate every specific transaction for the merchant to be able to review, and it would indicate whether or not it was a qualified transaction or a non-qualified transaction. In the case of an error being made, we'd certainly make sure we'd correct it. Yes, thank you.

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. Baumgartner and Mr. McTeague.

We're now going to the member for Burlington, Mr. Wallace.

Mr. Mike Wallace (Burlington, CPC): Thank you, Mr. Chairman.

Thank you for coming this afternoon. It's a very interesting discussion.

I'm going to stick to the TD approach, so if you want to get it out, I'm going to go over it.

The issue we've been hearing from merchants thus far is about how complicated this is, and you didn't make it any easier today. If I'm looking at the statement under summary of fees, is the interchange rate in any of these fees I'm seeing on the bottom here?

Mr. Jeff van Duynhoven: The interchange rate is not listed on there, but as we said earlier, it is the largest component of the fees that make up the Visa delivery rate.

Mr. Mike Wallace: So it's not listed in there. I took the \$824 and I have no idea what you do with the direct payment sales or the chargebacks—I know what they are, but I don't know what you do with them—or the returns. When I did the math, it came to 2.7%, but that does not include the interchange fee, is that correct?

Mr. Jeff van Duynhoven: There is no other fee. If you've taken the \$824, that is the total amount we have charged that particular merchant.

Mr. Mike Wallace: So that includes every fee—

Mr. Jeff van Duynhoven: It includes all the fees we would charge to the merchant.

Mr. Mike Wallace: So how do you treat, to the merchant, the direct payment sales of \$9,600? Do they get charged down here for the transaction of that for each one of those 224 transactions? Is it part of that down here?

Mr. Jeff van Duynhoven: Yes, so in the example we have summary of fees. You see an IDP, or Interac direct payment transaction fee. The example, at 8¢ a transaction times 224, is roughly \$18.

Mr. Mike Wallace: So for me to do the math, if I add up all the transaction numbers at the top, divide them by the \$824, it's approximately my cost per transaction, depending on what the transaction might be.

Mr. Jeff van Duynhoven: If you were trying to work it out to an average discount rate, then yes.

Mr. Mike Wallace: If I'm planning my business, I need to know approximately. I don't eat it; I have to pass it on to my customers, so I have to have an idea of what I'm paying so I can pass that on. The first fee, the Visa discount, goes to you, right?

Mr. Jeff van Duynhoven: All these fees come to us. We collect all these fees.

Mr. Mike Wallace: Yes, but this one goes to you. The transaction fee is for the 224, so that's the fee I'm paying, and it's \$0.08, right? I got that. That's your total. Your POS machine, is that \$35 a month?

Mr. Jeff van Duynhoven: Yes, so again, it's an example. It might range anywhere from \$20 to \$35 a month for the rental of the device. Again, as I said, it depends—

Mr. Mike Wallace: Can you buy them?

Mr. Jeff van Duynhoven: You can buy them, yes.

Mr. Mike Wallace: What are they worth?

Mr. Jeff van Duynhoven: Most customers like the opportunity to rent from us because we have what we call a four-hour service promise, so we promise, at least 90% of the time, that if you call us and your terminal breaks down, we'll be on-site with a service technician. We have 250 service technicians across the country.

Mr. Mike Wallace: Okay.

I understand the taxes. The Visa assessment fee...and that's a percentage negotiated between you and the retailer?

Mr. Jeff van Duynhoven: In our case, it is the straight pass-through of the Visa assessment fee. Visa charges us six basis points plus GST, and that's what the 6.3 basis points reflect.

Mr. Mike Wallace: The next one is the discount rate adjustment fee. It's \$68.15 in your example. And you explain what that is three pages later.

Can you tell me the difference between Canadian Infinite standard—Infinite electronic, I guess that is—commercial standard, and commercial...? What's the difference between standard and electronic?

Mr. Jeff van Duynhoven: There are different types of transactions. I mentioned the way the merchant processes those transactions.

An electronic transaction is either one that is swiped—so the card is there—or one that is a chip transaction, where the chip is inserted into the terminal. For those, we know the card is there, so they're less likely to be turned down.

Standard transactions are those for which the card is not present. I mentioned that e-commerce transactions are standard, because you're purchasing at a website and the card is not physically at the merchant's location. So Visa actually has differential interchange rates for those transactions. And we break out all of those card types, where we've charged a premium for those card types—

• (1710)

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. Wallace, and thank you very much, Mr. van Duynhoven.

[Translation]

Mr. Carrier.

Mr. Robert Carrier: Good afternoon.

I want to come back to the issue of premium cards. I have mentioned the Australian model that has been recommended by the coalition of retailers. You said that you do not approve of that model because you are more in favor of free competition.

Since you only process payments... Credit cards meet a definite need and I believe you will continue to use them because they are very useful. So, I think you would not lose anything if the interchange fees were fixed.

Why are you not in favor of a maximum rate set by regulation?

[English]

Mr. Jim Baumgartner: Sure, yes. The different products that are out there, including commercial card products, etc., have different behavioural characteristics. This is my view. I think there is a place for different interchange levels in the system to incent different types

of behaviour. I also believe that absent, including in the case of American Express, in any of those discussions is the fact that we would have an unintended consequence if we imposed the Australian example. And that could be that the issuing community decides it's in their shareholders' best interests to issue American Express cards as opposed to Visa or MasterCard cards. The fees that are charged on those cards and the fees that the issuers would receive from those cards would be dramatically higher even than what they're currently receiving today.

And so I think a combination of those two things, as well as—and I don't know for sure—the potential for decreased innovation with things like contactless, for example, and things like the chip, which again, I believe, is a very good thing for the Canadian consumer just from a data integrity perspective.... Examples like these, I think, are driven in a free market, and I don't know if, in a more constrained market, we'd have that type of innovation here.

[Translation]

Mr. Robert Carrier: The way you are explaining it, it seems well and good but retailers say that they are the ones who will have to bear the higher rates for the use of premium cards. They are the ones faced with the problem, not you. It is easy for you to talk about free competition and to offer various gadgets to sell more cards and to increase their use but there is definitely a problem for retailers. What is your reaction to this?

Are you opposed to including American Express in the regulation of interchange fees?

[English]

Mr. Jim Baumgartner: Sure. With respect to the premium cards, one of the things I did look at more recently was the difference in behaviour. Do the holders of premium cards have different behavioural characteristics? And the answer is they actually do.

I think that MasterCard mentioned that they have an average spend in their portfolio of \$24,000 apiece to qualify for a premium card. And when I looked at the behaviour across our merchant categories—and this was only the last month, so it's only a month's worth of data—the average transaction size of those particular cardholders was markedly higher. It was a lot higher than I suspected it would be. The lowest was in the gas station category, where their cards were a little bit bigger, but they didn't spend that much more; it was a little bit more on food; and it went all the way up to as high as 40% in certain merchant categories.

So it is clear that those particular customers are bringing more value to merchants. But at the end of the day, it's costing merchants more money than they're used to paying. In large part, I think that's why we're here today, because the increases were much more aggressive than I think anyone was expecting, and no one really had a good sense of how many premium cards there actually would be. The merchants couldn't budget for them, and I think that has definitely caused some issues. I think your association is a great example of those issues.

• (1715)

The Co-Chair (Hon. Michael Chong): Thank you very much, Mr. Baumgartner.

[*Translation*]

Thank you, Mr. Carrier.

[*English*]

That ends our rounds of questions and comments from members of the committee.

Thank you very much to our witnesses for appearing. Your testimony will be useful to us in forming our report.

We're going to suspend for two minutes to allow witnesses and audience members to depart so we can return in camera to discuss future committee business.

The meeting is suspended.

[*Proceedings continue in camera*]

Published under the authority of the Speaker of the House of Commons

Publié en conformité de l'autorité du Président de la Chambre des communes

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