



**Consumers' Association of Canada
Association des consommateurs du Canada**

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**Written Submission to the Joint House of Commons Finance
and Industry Committee Study of Credit Card Interchange
Fees and the Debit System in Canada**

June 22, 2009

Thank you for the opportunity to provide our views on credit card interchange rates and Canada's debit payments system. Many financial sector organizations and retail groups coming before your Committee have purported to speak on behalf of the consumer's interest. Therefore, we felt it was important for an organization that actually represents consumers to comment on the likely impact of potential changes to payments systems in Canada.

Given the importance of the consumer perspective to these discussions, I would like to reiterate our offer to appear before the Committee.

About the Consumers' Association of Canada

The Consumers' Association of Canada (CAC), founded in 1947, is an independent, not-for-profit, volunteer-based charitable organization. Our mandate is to inform and educate consumers on marketplace issues, to advocate for consumers with Government and industry, and work with Government and industry to solve marketplace problems.

CAC focuses its work in the areas of food, health, trade, standards, financial services, communications industries and other marketplace issues as they emerge. A national volunteer organization, CAC maintains a national secretariat in Ottawa with regional offices in Vancouver, Edmonton, Saskatoon, Winnipeg and Montreal.

The mission of the CAC is to represent and articulate the best interests of Canadian consumers to all levels of Government and to all sectors of society by continually earning recognition as the trusted voice of the consumer on a national basis.

Issues Before the Committee

We would like to address the consumer impact of a number of issues that have been raised during the Committee hearings.

Credit Card Issuer Practices

The CAC has made a number of longstanding recommendations relating to credit card issuer practices. Our focus has been to ensure consumers receive transparent and easy to read information about the terms and conditions of their card so they can make informed decisions about the best credit card product that suits their needs. We also referenced some business practices that we believe need to be standardized in order to reduce consumer confusion regarding the cost of carrying a balance on a credit card. For example, we have long advocated for standardized grace periods in credit card agreements as a way to lessen consumer confusion.

Standardized collection practices have been another area of focus. The CAC believes consumers deserve to have a national standard in terms of the treatment that they can expect when financial institutions need to collect outstanding debts.

Finally, the CAC is concerned that the interest rates on credit cards often do not appear to have been lowered to correspond with a lower Bank of Canada prime rate. However, we do not believe the solution to this is price regulation. We believe the role of the Government is to ensure that consumers are given the tools they need to make informed decisions. That is why the CAC has not recommended capping or regulating interest rates charged by financial institutions. It is our view that such regulation would actually harm consumers rather than help them, since it could unnecessarily restrict consumer choice.

The CAC position is that consumers are better served in terms of lower prices and increased choice and convenience when Governments encourage competition as opposed to trying to put caps on price.

On this basis, we welcomed the Finance Minister's recent proposals for regulation of credit card issuer practices because they will address the key consumer concerns in the market without having unexpected adverse consequences for consumers. In fact, we would welcome the extension of the Minister's proposals to retail credit cards. These cards, which have the highest interest rates and are very easy for consumers to access, seem to operate outside any Government regulatory framework.

Interchange

We have followed the Committee hearings on interchange with interest and wish to make the following comments.

1. Interchange fees are not fees that consumers pay.

It has been suggested by the merchant community that interchange fees are paid by consumers. This is not actually the case. It is instead a fee paid by the various parties involved in a credit card transaction; i.e. issuers, acquirers and retailers. We would consider interchange a cost of doing business like any other.

These fees may be a concern to retailers, but that does not extend to consumers. The fees consumers are interested in are those they pay directly, like interest, annual fees, or fees for withdrawing cash from an ATM. We do know from the Australian experience that consumer fees in that country increased when regulation forced interchange lower. Therefore, we find it quite disingenuous when the retail lobby argues for lower interchange to protect consumers when they know it is only going to result in higher costs for consumers in other areas. The only benefactor in such a scenario is the retailer, as discussed in more detail below.

2. The CAC does not believe that merchants will pass on any decreases in interchange fees.

The retailers have suggested that consumers should be concerned about interchange because we ultimately end up paying for any increases. By that logic, consumers should

look forward to price reductions if interchange is lowered. I would point out, however, that the retail witnesses appearing before your Committee have gone to great lengths to explain why that may not actually be the case. In fact, there have been witnesses before your Committee, like grocery retailers, who have received reductions in their interchange rates, yet they still warn of having to increase prices.

As an interesting aside, I would point out that Loblaws, Sobeys and Metro have all posted huge profit increases in the first part of this year, which is no small accomplishment in a recession. Groceries are a necessity of life and I would encourage the Committee to look at grocery store pricing in the future. That is an area where consumers would be very well served by greater price transparency.

In fact, the retailers have suggested that interchange be priced at cost “plus a reasonable rate of return”, which is largely undefined, but clearly something the retailers think they or the Government should have a role in setting since they are the ones who are paying it. To use the retailers’ own logic once again, might I suggest that retail prices be capped at cost “plus a reasonable rate of return”. Given that consumers are the ones who pay retail costs for life essentials like food and clothing, I look forward to the retailers inviting organizations like ours to work with Government to determine what that reasonable rate of return should be.

Returning to the issue at hand, the CAC does not believe merchants will pass along any savings from interchange reductions to consumers. Instead, those reductions will be pocketed by the retailers. This is exactly what happened in Australia when the Reserve Bank moved to regulate interchange fees. Merchants did not pass fee reductions on to consumers. In fact, despite the interchange reductions, many merchants took advantage of new rules that allowed surcharging. Consumers who wished to pay by credit card were presented with a new cost, meaning costs to consumers in Australia actually went up as a result of interchange decreases.

Here in Canada there is already evidence that when merchants receive cost savings they do not always pass it on to the consumer. The best example was in 2007 when Canada saw a rapid appreciation of its dollar to a point where it was trading at or above par compared to the American dollar. It was well documented at the time that many retailers did not adjust their prices to account for the dollar’s appreciation.

For example, many book retailers continued the practice of charging Canadian consumers significantly more for the same book than the price charged to U.S. consumers. Retailers of items such as furniture, appliances and clothes continued to charge much higher prices at their stores in Canada than in the United States, even though the Canadian dollar had risen from \$0.75 to par. Our concern is that with the recent rapid appreciation of the dollar we will once again see evidence of merchants not passing on their savings to consumers in the form of reduced prices. This is an area the Committee should consider.

3. Cash discounts

Cash discounts have been presented as one possible solution to this issue. It is amusing to observe witnesses from the retail community suggest cash discounting is too difficult for their employees to grasp. While I am not an expert in cash register technology, these devices are highly sophisticated today and I suspect they could easily be programmed to offer a discount for cash at the press of a button. Under such a scenario, all the clerk would need to do is a) recognize a cash payment and b) hit the right button. That would not seem to require months of training.

It is also interesting to note that retailers in many cases have made it increasingly difficult to pay with cash, in effect forcing people to electronic payments. Examples include pay at the pump gas stations or self check-out at the grocery store. Both technologies allow significant savings when it comes to staffing, though there is no evidence those savings have been passed on to the consumer who, ironically, now has to do all the work. Perhaps retailers should be offering discounts for consumers who use one of these cost-saving payment methods.

Finally, the issue of surcharging for credit card purchases has come up in the hearings. This is an area where the Government should tread carefully. The CAC is opposed to surcharging on a credit card transaction. One clearly displayed price should apply regardless of the method of payment. There would need to be real scrutiny over any suggested retailer practices in this area.

To put that in context, I often take a cab in from the airport when I am in Ottawa. The ride downtown costs about \$30. If you pay by credit card or debit, there is a \$1.50 surcharge. Accepting a generally agreed upon interchange rate of 2% for a credit card, the cost to the cab company for that transaction is \$0.60. In other words, they make a \$0.90 profit on the surcharge alone. It is even worse for debit, which has a flat cost of around \$0.12 per transaction, meaning the cab company is pocketing an extra \$1.38 in profit from the surcharge.

These types of merchant practices have not been examined by the Committee. It is why we bristle when some of the merchant lobby organizations are claiming to speak on behalf of consumers. They are in no position to do so until their own pricing practices are put under scrutiny.

4. Reward programs

Reward programs exist for a reason: because consumers like them. They have become widespread across the retail landscape and are offered not just by credit card companies, but by retailers directly as well. Many Canadians collect rewards as a way to “fund” the acquisition of goods and services. Rewards become even more important during an economic downturn since they maximize the purchasing power of every dollar.

Canadians redeem rewards points to acquire hundreds of millions of dollars of good and services each year. For example, Canadian families routinely redeem rewards as a way to purchase airplane travel and hotels for family vacations, groceries, hardware purchases, movies, and even mortgage payments. The benefit and value consumers receive from collecting and redeeming rewards points has been lost in the discussion of credit card interchange fees before your Committee.

All witnesses can agree that interchange is used to fund at least some portion of the rewards points being provided to consumers. Common sense and evidence from Australia suggest that if interchange is artificially lowered by Government controls then consumer rewards points will decline as well. Lower rewards points, combined with the fact that merchants will not pass on any savings on reduced interchange, means any Government intervention to cap interchange would result in consumers being substantially worse off.

There is no consumer benefit under such a scenario. In fact, you are likely to face irate consumers asking why the Government and large retailers conspired to take away their reward programs.

Debit Transactions

We have monitored the discussion about Canada's debit system and the recommendation by some that the Government limit competition in the debit sector. Our consistent view on Government regulation is that it should encourage competition and choice as opposed to limiting it. There are also tangible benefits for consumers from the proposed entry of MasterCard and Visa into the debit market, such as international usage and on-line purchasing. These benefits should not be dismissed.

Conclusion

We appreciate the interest of the Committee in these important issues. We welcome Minister Flaherty's recent nine-point plan for improved credit card regulation, transparency and education. We believe these changes, once implemented, will result in real and tangible benefits to consumers.

However, we are quite concerned with the proposal by some retail groups to regulate interchange fees. We believe legislated fee reductions for retailers will not be passed down in the form of lower prices to consumers. In fact, experience in Australia suggests that consumers may see higher costs as merchants implement more widespread surcharging for the use of credit cards. Experience in Australia also suggests that price caps on interchange will lead to lower rewards benefits and higher fees – things that directly affect the consumer.

As the Committee prepares its report, I hope that you will consider the views of the Consumers' Association of Canada, rather than other groups that claim to speak on behalf

of consumers. I would also encourage the Committee to take a closer look at a wide range of retailer practices, most of which have avoided public scrutiny for decades.