

Unclassified

English - Or. English

13 September 2021

**DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE**

**LATIN AMERICAN AND CARIBBEAN COMPETITION FORUM - Session III: Competition
and Payment Card Interchange Fees**

– Contribution from Chile –

20-22 September 2021

The attached document from Chile (FNE) is circulated to the Latin American and Caribbean Competition Forum FOR DISCUSSION under Session III at its forthcoming meeting to be held on 20-22 September 2021, via a virtual Zoom meeting.

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JT03480806

Session III: Competition and Payment Card Interchange Fees

- Contribution from Chile (FNE)¹ -

1. Introduction

1. Payment card schemes in Chile began with the incorporation, in 1989, of *Sociedad Interbancaria Administradora de Tarjetas de Crédito S.A.* [Interbank Credit Card Administrator], subsequently, Transbank S.A. (“Transbank”), which began operating in 1991. The development of this industry can be divided into three main stages: (1) an incipient period, in which the main issuers launched a joint venture to create an acquiring operator, under a three-party system; (2) a stage of transition towards a competitive model favoured by the Chilean institutional community, both the financial sector and proponents of free competition; and (3) a recent period of major competitive dynamism as a result of the industry’s transition to a four-party system. Each of these stages has posed different challenges and risks to competition, requiring the intervention of the Chilean authorities in charge of protecting competition.

2. Stage one: a three-party monopoly system

2. In 1991, seven banks and financial institutions in Chile applied to the Central Preventive Commission² for authorisation to jointly develop the payment card scheme business through a subsidiary company: Transbank S.A. The *Fiscalía Nacional Económica* [National Economic Prosecutor’s Office – FNE] intervened in this proceeding, indicating that this joint action did not affect free competition given the low penetration, at that time, of this payment method and the high costs of developing a merchant network.³ In line with these considerations, the Commission authorised the requested joint action and instructed the FNE to monitor its evolution to avoid monopolistic practices in this market.⁴

3. During this period, the industry was organised according to a three-party system in which, in line with regulations, card schemes could only be operated by an issuer, or by a group of issuers through a subsidiary company. Under this system, each time a payment was made, the transaction information was sent directly from the Transbank point of sale (POS) to the issuer of the card used to make the purchase. The issuer would then verify that the required amount was available in the current account (if a debit card was used) or as available credit (if a credit card was used), and that information would be sent to the operator, who would approve the transaction. In other words, the infrastructure formed a fully closed technological loop between the sole operator in Chile and the issuers, most of which were part owners of the operator.

¹ Contribution of the *Fiscalía Nacional Económica* [National Economic Prosecutor’s Office – FNE].

² The Central Preventive Commission is one of the commissions that merged to become the current *Tribunal de Defensa de la Libre Competencia* [Competition Tribunal – TDLC], which began operating in 2004.

³ Report submitted through Regulation No. 226 dated 4 April 1991.

⁴ Ruling No. 757/262 of 1991, confirmed by Ruling No. 898/262 of 1994.

4. In 2001, after 10 years of monitoring and controlling the activities of Transbank, the only card scheme operator in Chile, the FNE submitted a petition to the Central Preventive Commission; then, in 2003, it applied to the recently established *Tribunal de Defensa de la Libre Competencia* [Competition Tribunal – TDLC] for an injunction against the company for antitrust violations. In the course of those proceedings, a partial settlement was reached with Transbank (the “settlement”), by virtue of which the maximum merchant discount rate that the company could charge was established. The settlement also imposed obligations such as establishing public, general, objective and non-discriminatory rates, and granting free access to merchants wishing to accept cards as a means of payment.⁵ To comply with these obligations, Transbank was required to submit a *plan de autorregulación* [self-regulation plan], which had to be approved by the TDLC and supervised by the FNE. Moreover, a price-setting scheme was imposed on Transbank, due to its monopolistic position.

5. With respect to matters not covered by the settlement, the TDLC accepted the FNE’s request, imposing a fine of 1 000 monthly tax units on Transbank for abusing its monopolistic position to engage in discriminatory conduct.

1. Stage two: laying the foundations for a competitive industry

6. In 2013, after a series of investigations into Transbank’s enforcement of the self-regulation plan,⁶ the FNE initiated a non-contentious consultative procedure through the TDLC to review the authorisation that had been given to the banks to jointly participate in Transbank, requesting that this authorisation be rescinded. Although the TDLC rejected the FNE’s request, judging that it was based on contentious information which could not be used in a consultative procedure,⁷ it initiated, on the same day, a Regulatory Recommendation Procedure.⁸ The objective of this procedure was to propose legal and regulatory reforms to the authorities, as the information presented by the FNE revealed a series of competition problems that required a structural solution.⁹ These problems related to services involving the use of credit and debit cards as means of payment and, in particular, regulatory barriers that inhibited new card operators from entering the market.

7. This proceeding made it possible to study the payment systems industry as a whole, with the active participation of various industry actors, the financial sector authorities and, in particular, the FNE, which opened an investigative proceeding to gather new information and commissioned reports from national and international consultants. These reports

⁵ Settlement dated 5 April 2004, approved by the TDLC on 13 April 2004.

⁶ Investigations No. 815-06, No. 901-07, No. 921-07, No. 1936-11, No. 2035-12 and No. F-24-13.

⁷ Chile’s TDLC deals with different types of proceedings. For the purposes of this paper, the most relevant are: i) contentious proceedings, aimed at hearing and resolving anticompetitive practices of market agents, which may result in the offender being sanctioned; ii) non-contentious or consultative proceedings, whose purpose is to bring certain facts or actions to the attention of the court so that it may judge whether or not they are contrary to free competition and, if so, adopt non-punitive measures to correct them; and iii) regulatory amendment proceedings, whose purpose is to enable the TDLC, if it sees fit, to propose to the President of the Republic, through the relevant ministry, the enactment, amendment or repeal of legal provisions to promote competition. Decree Act No. 211 of 1973, Article 18.

⁸ Initiating Resolution dated 4 April 2014 on page 1 in case No. ERN (*expediente de recomendación normativa*) [regulatory recommendation proceeding] 20-14.

⁹ Up until that point, the Compendium of Financial Regulations issued by the Central Bank of Chile had defined the operation of payment card schemes as an activity to be carried out by one or more issuers, either in their own name or by delegating the activity to a third party. This definition was recognised by the TDLC in Regulatory Amendment Proposal No. 19/2017, para. 423.

revealed three major problems:¹⁰ i) the three-party system discouraged competition in payment card schemes as only acquirers vertically integrated with issuers could participate and, in Chile, the main banks acted jointly with the only operator in the market, making it necessary to establish the conditions to migrate to a four-party system; ii) the international card brands had established a series of rules for merchants – through Transbank – that reduced competition between the different types of cards; and iii) the move to a four-party system would require the authorities to regulate interchange fee pricing, as shown by international experience in the matter and considering how the European Union and Australian markets operate.

8. Finally, after almost three years of discussions in the framework of this proceeding, the TDLC issued its Regulatory Amendment Proposal, accepting most of the solutions proposed by the FNE¹¹ and recommending to the authorities a series of amendments. These were: i) to clearly separate card scheme operators from card issuers (which up until then, by law, had to be vertically integrated); ii) to prohibit banks acting jointly in the card scheme market; iii) to prohibit card brands from applying the “no acquiring without issuing” (NAWI) rule¹² and the “no surcharge” rule;¹³ iv) to make the necessary legal and/or regulatory changes for the Chilean system to operate under a four-party system; and v) to have interchange fees regulated by the authorities.

9. These recommendations laid the foundations for a more competitive industry, which ultimately materialised through a regulatory amendment issued by the Central Bank of Chile. This amendment repealed the rule requiring card scheme operators to maintain delegation contracts with issuers. It also obliged all market actors to establish interconnection mechanisms between issuers, the card brands and the authorised card scheme operators,¹⁴ so that whichever card scheme operator is used by the merchant involved in the transaction, the transaction information is channelled to the card companies and then on to the issuers, who verify the amount for payment and communicate this information back via the same digital path. The conditions for the industry to migrate to a four-party system were thus established at the regulatory level.

2. Stage three: competition challenges in a four-party system

10. A year after the TDLC made its recommendations, Banco Santander, one of Transbank’s main shareholders, announced its decision to sell its stake in the card scheme operator and its intention to compete with it through its own operator (this company, called Getnet, entered the market in 2020 and is now operating in Chile). In addition, in 2017, a payment card scheme operator called Multicaja, not linked to any issuer in Chile, entered the market with the aim of competing with Transbank.

¹⁰ FNE report dated 2 June 2014, page 800 in case No. ERN 20-14, which refers to the background information contained in its Consultation Brief dated 27 December 2013, page 1 in case No. NC 418-13.

¹¹ Regulatory Amendment Proposal No. 19 dated 12 January 2017, page 1925 in case No. ERN 20-14.

¹² This rule, imposed by the card brands, required any bank wishing to act as an acquirer to also become an issuer, either itself or through a related company.

¹³ In accordance with this rule, imposed by the international card brands, “merchants may not charge a different price for a good or service according to the means of payment used for the transaction. In particular, this means that they may not charge more for credit or debit card transactions than for cash or check transactions”. This rule was defined by the TDLC in Regulatory Amendment Proposal No. 19.

¹⁴ Chapter III.J.2 of the Compendium of Financial Regulations of the Central Bank of Chile.

11. The migration to the four-party system generated new challenges to competition, which the competent authorities dealt with through various investigations and by bringing various proceedings before the TDLC.¹⁵ These challenges were: i) ensuring the transition of Transbank's self-regulation plan for adapting its pricing, and the rules contained therein, to the new four-party system; ii) ensuring sufficient interoperability between the different actors in the system to allow any authorised operator to develop its business; iii) limiting the rules imposed by the card brands that were disincentivising competition; and iv) regulating the interchange fees that were set – now in an four-party system – by the card brands.

12. With respect to the first of these challenges, the FNE pointed out to Transbank that, despite the industry's migration to a four-party system, it was still subject to the provisions of the settlement, given its supra-competitive position, and therefore had to adapt its self-regulation plan.¹⁶ As a result of these negotiations, FNE and Transbank entered into an extrajudicial agreement which had two objectives: i) to regulate the acquiring margin rates charged by Transbank, to keep costs low;¹⁷ and ii) to establish transitory rates to protect merchants from rising costs due to the increase in interchange fees.¹⁸ However, the TDLC rejected this extrajudicial agreement, ruling that the matter should be heard in a non-contentious proceeding that would allow all industry actors concerned to participate.¹⁹ In response, Transbank initiated a consultative procedure with the TDLC,²⁰ presenting a new, moderately priced tariff scheme, following the guidelines of the extrajudicial agreement, although the agreement is still pending resolution.²¹

13. With respect to the challenges of interoperability, the FNE opened investigation No. 2515-18 to gather information from issuers, card brands and card scheme operators in order to monitor the status and progress of technological developments that would allow interoperability, which is key for the industry to operate in a four-party system.²² Currently, conditions for interoperability are being discussed and analysed in non-contentious proceedings at the TDLC. The FNE has made a report to these proceedings on the technological progress achieved thus far: the work is almost complete, although a few specific functionalities still need to be added.²³

¹⁵ Investigations No. 2515-18, No. 2605-20, No. 2620-20, No. 2634-20 and No. 2643-20.

¹⁶ To ensure that Transbank complied with the settlement and adapted its self-regulation plan to the four-party system, the FNE opened investigation No. 2605-20.

¹⁷ In the three-party system, Transbank determined the merchant discount rate according to the tariff scheme established in its self-regulation plan. However, in the four-party system, the company can only determine one of the components of the merchant discount rate – the acquiring margin – since the interchange fees and the costs of the card brands (licenses, payment switch, etc.) are determined by those brands.

¹⁸ Extrajudicial Agreement dated 31 March 2020 between the FNE and Transbank, submitted for approval by the TDLC in case No. AE 17-20.

¹⁹ Resolution of the TDLC dated 29 April 2020, page 459 in case No. AE 17-20.

²⁰ Consultation filed by Transbank on 12 May 2020, in case No. NC 463-20.

²¹ To analyse the new tariff scheme presented by Transbank, the FNE opened investigation No. 2620-20. On the basis of this investigation, the FNE presented a legal-economic report on the implications of the acquiring margins established by Transbank and defined some rules that the company would have to observe in its commercial relations with issuers, other operators, merchants and payment processing providers.

²² Initiating Resolution of investigation No. 2515-18 dated 8 May 2019.

²³ Report of the FNE dated 9 November 2020, page 99 in case No. NC 474-20.

14. With respect to the rules established by the card brands, the FNE has asked the TDLC, in line with the recommendations made by that court in its Regulatory Amendment Proposal, to: i) eliminate the NAWI rule, to remove any artificial barrier to entry into the card scheme market; ii) repeal the no surcharge rule, to allow merchants to set their prices freely; and iii) partially prohibit the “honour all cards” rule,²⁴ so that merchants have full discretion to choose the types of cards they wish to accept. A decision on this case is still pending.

15. Finally, regarding the regulation of interchange fees by the authorities, the FNE participated in a process initiated by the TDLC, by virtue of its office, to temporarily regulate the level of interchange fees, until the level was established by law.²⁵ As part of this process, discussions were held on guidelines for quantifying interchange fees, the methodologies applied at the international level, and the potential impact on consumers of a fixed-level scenario as opposed to a deregulated scenario, such as the one currently in place.²⁶ However, on 6 August 2021, Act No. 21.365 came into force, creating a committee to set interchange fees. The committee includes a representative of the FNE and it has six months to issue its first regulation. With this law having come into force, the TDLC declined to exercise its regulatory powers in this matter.

3. Conclusion

16. The payment systems industry in Chile, after many years of monopoly, has benefitted from repeated and robust interventions by the FNE and the TDLC to protect consumers from harm and open the market to competition. There are currently five card scheme operators in the country and new companies are expected to enter the market, generating a considerable increase in competitive pressure in recent years. This trend is expected to develop even further with the introduction of new products, such as prepaid cards, and new technologies, such as e-wallets and QR code payments, by new operators and financial technology companies.

17. Moreover, although migration to a four-party system initially entailed a considerable risk of price rises due to the imposition of interchange fees arbitrarily set by the card brands, Chile now has a public institution in charge of setting these rates in a way that supports a competitive, inclusive, transparent payment card market, with strong penetration, and whose objective is to safeguard the efficient and safe operation of the retail payment system.²⁷

²⁴ This rule, imposed by the international card brands, requires operators to oblige merchants that receive card payments to accept all cards in the system, without exception.

²⁵ Initiating Resolution dated 3 December 2020, page 1 in case No. NC 483-20.

²⁶ FNE report dated 12 January 2021, page 127 in case No. NC 483-20.

²⁷ Article 3, para. 2 of Act No. 21.365.