



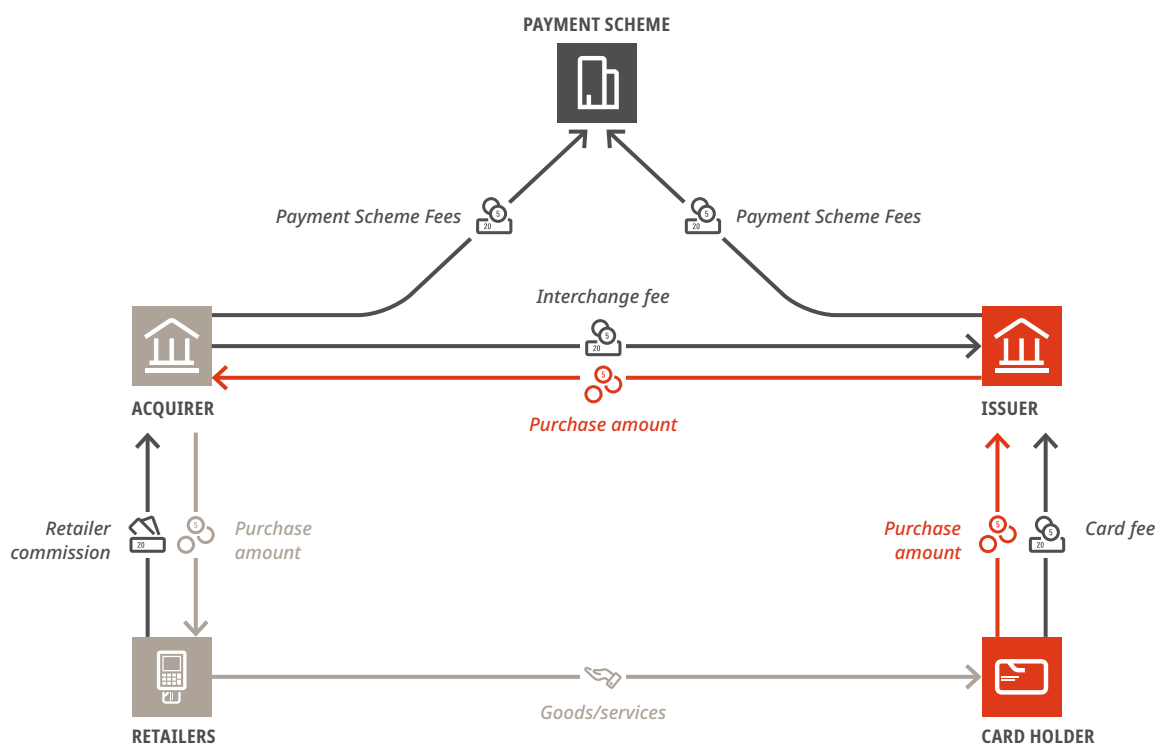
Four-Party Model, Fee Structure and Interchange in Debit Card Business

Functionality, Importance and Role

To allow non-cash payments, multiple players are required. Fundamentally, it is the card payment system (payment scheme) that operates as network and licensor.

The four-party model (e.g. Mastercard and Visa)* is most commonly used. Here, four parties are connected via the payment scheme.

Four-Party Model



* Other payment schemes, such as PostFinance, JCB, Diners Club or American Express are based on a three-party model, where the acquirer is also the issuer and therefore interacts simultaneously with the retailer and also the card holder.



The Parties Involved

Payment Scheme

A company that offers card products and services and defines the card brands, processing rules and fee structures (interchange and payment scheme fees) associated therewith. It also controls the standards and carries out the central processing of card transactions, such as authorization, clearing and settlement.

Processor (Acquiring & Issuing)

A company that supplies contractually agreed card business services, in particular, the processing of card transactions, for one or more banks or institutions. If the issuer and acquirer or their processor are identical, the majority of the transactions will normally be processed “**on-us**” (with the processor’s infrastructure), and they will not be processed via the payment scheme.

Issuer

A bank or institution that issues cards to its customers (card holders). It manages its customers’ card accounts, authorizes card transactions and guarantees payment settlement of valid card transactions for the acquirer.

Card Holder

The holder uses the prepaid, debit or credit card as a payment means.

Acquirer

The bank or institution that has a with a contractual business relationship with the retailer and bills the card transaction data submitted by the retailer to the respective issuer via the relevant payment scheme.

Retailers

Physical points of sale (POS) or virtual webshops (e-commerce) that accept card payments.



Fee Structure

The participants are involved in the cost and income structures as follows:

Payment Scheme

The payment scheme levies license, processing and service fees (payment scheme fees). As a rule, the license fees are fixed, while the processing fees are based on card transactions and the number of cards. Service fees are also charged for monitoring fraud, managing the bank identification number (BIN) or market development.

Processor (Acquiring & Issuing)

The processor will invoice the acquirer or issuer fees for transaction processing (authorization & clearing) and the operation of transaction processing systems as well as possible additional services (such as those related to risk and fraud prevention).

Issuer

The issuer may charge card holders annual fees for the card. The issuer also receives an interchange fee from the acquirer as a fixed and/or volume-dependent fee for the card transaction. The issuer pays license fees to the payment scheme. The payment scheme therefore covers its costs for maintaining the regulations, operation and development of the payment infrastructure (such as security) and for innovation and marketing.

Card Holder

As a rule, the card holder pays the issuer an annual fee for the card. Depending on the type of use and transactions, the card holder will be charged additional fees.

Acquirer

The acquirer charges the retailer a merchant service charge (MSC) per card transaction as a fixed or percentage fee of the transaction amount. The MSC contains the interchange fee (for the issuer) and the payment scheme fees and comprises all the acquirer's costs for processing the transaction. Additional transaction-dependent fees are possible. Similarly to the issuer, the acquirer pays license fees to the payment scheme.

Retailers

The retailer pays for the entire infrastructure, pays any technical partners needed, such as payment service providers (PSP), assumes the costs for the data transmission and delivers the merchant service charge (MSC) including the interchange fee to the acquirer. Additional transaction-dependent fees are possible.



Acquirer Pricing Models

Acquirers use different pricing models for their retailers. These are largely dependent on the size of the retailer (transaction volume, number of transactions) and can consist of several components.

The most commonly used models are the following:

“Flat pricing” (also known as “packs” or “bundles”) – typically for the smallest retailers:

- = a static monthly fee (“subscription”)
- = a certain number/volume of transactions “free” (settled with the monthly fee)
- = a % and/or fixed fee is applied to the additional transaction volume above the number/volume

“Blended” – for smaller retailers:

- = a fee per brand % and/or fixed

“Blended Plus” – for medium-sized retailers:

- = a basic fee per brand % and/or fixed
- = surcharges (depending on the cost drivers) for certain “scenarios” such as:
 - Ω transactions with commercial cards – surcharge of % and/or fixed
 - Ω transactions with non-EU cards – surcharge of % and/or fixed
 - Ω manually recorded transactions

“Interchange Plus Plus” – for large and very large (key account) retailers:

- = a dedicated fee for interchange (replicates the effective interchange costs)
- = a dedicated fee for payment scheme fee (as a rule, an “approximation” of effective payment scheme fees)
- = a dedicated acquirer fee (covers the acquirer costs and the acquirer margin)

Interchange

History, Sense & Purpose

Definition

The interchange fee is a card- and volume-dependent transaction fee that is charged by the acquirer to the retailer and paid to the issuers.

The interchange fee serves as a key compensatory instrument in the four-party model. It allows costs/benefits to be distributed properly among all participants (card holders, issuers, acquirers and retailers) and also contributes to an issuer issuing cards and card holders being motivated to use them.

With the interchange fee, the issuer covers part of their costs for:

- **Customer support:**
Production/issue/renewal of the card, managing the card account, operating customer service.
- **Transaction processing:**
including authorizing payment or clearing and settlement.
- **Combating fraud and the consequences of fraud:**
including monitoring card transactions, refunds due to improper charges by the card holder or refunds to the retailer in the event of fraudulent purchases of goods or services (chargebacks)
- **Development and market launch of product innovations.**

Parameters

The interchange fees are determined by the payment schemes. There are the following regional interchange fee variants:

- The **domestic multilateral interchange fee (DMIF)** is applied if the payment takes place in the country in which the card was issued.
- The **intra-regional interchange fee (within Europe)** is applied if a European card holder makes a payment in another European country.
- The **intra-regional interchange fee** is charged if card holder from outside Europe makes a payment with the card.

For domestic transactions, the interchange fees in Switzerland are set by Mastercard and Visa. Only domestic Maestro transactions are not subject to an interchange fee, as the interchange fee for Maestro is set at zero in Switzerland.

Interchange fees are set as a fixed amount or percentage of the transaction amount. They vary, among other things, according to the product (e.g. credit, debit, business, gold or platinum), type of transaction (e.g. contactless, chip, magnetic strip), sector (e.g. retail trade, gas stations, airline companies, public enterprises), security standard (e.g. 3DS, PIN entry), amount or geographical region.

Interchange fees for automated teller machines are prevalent. There, as a usage fee, they flow – contrary to the practice in card systems – from the issuer to the operator of the automated teller machines (site bank), whose automated teller machine the card holder uses to withdraw cash.

Trend

The pressure to reduce interchange fees has been an issue throughout the world for years and is increasing steadily. In particular, the EU set the upper limit for credit and debit cards at 0.3% and 0.2% respectively with its Interchange Fees Regulation (2015). The cross-border POS debit card interchange for transactions with retailers in the EU by non-EU card holders (including Swiss customers) has also been capped at 0.2% for the next 5 years.

The credit card interchange fee charged was also set at 0.44% by Visa and Mastercard in consultation with the Swiss Competition Commission (COMCO) in 2017 as a consequence of the regulated interchanges in the EU.

Interchange in Switzerland with Debit Mastercard and Visa Debit

The fact that Maestro does not have an interchange in Switzerland is a special case.

Following the market launch of V PAY in 2014, COMCO allowed an interchange for this debit card. This was done with the intention of providing start-up aid for the product launch. COMCO also allows interchange for national POS transactions for the new generation of debit cards, namely Debit Mastercard and Visa Debit. However, this arrangement is limited to 3 years or 15% market share, at which point COMCO will reassess the situation.

