

# Consumers are being fleeced by card currency conversion charges

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Open, general-purpose card schemes such as MasterCard and Visa were the greatest payments innovation in the 20th century. Consumers take for granted the enormous convenience and security of being able to pay, get cash and access credit worldwide.

The early 21st century is enjoying an unprecedented tsunami of payments innovation including mobile acceptance provided by ballyhooed Square and iZettle, UK banks' P2P payment system Paym, cryptocurrency Bitcoin, mobile-payments phenomenon M-PESA and a raft of digital wallets.

Competition and buyers tending to their interests in free markets reward firms delivering value-creating innovation and punish those that don't.

There are however unfortunate exceptions where, because of inadequate disclosure there's a large information asymmetry between parties, competition can produce perverse results. Dynamic currency conversion (DCC) is a case in point. It lets travellers using credit and debit cards pay in their home currency for which they pay a hefty 3 to 4% - often higher, foreign-exchange markup. A London hotel or restaurant invites a French tourist to pay in euros, he does, feels good, and is none the wiser he's been fleeced.

Merchant acquirers compete fiercely in providing card acceptance to merchants. Some merchants love nothing better than to be able to trick one-time foreign customers into paying 4% more, which is shared with their merchant acquirer and DCC specialist. Consequently competition between merchant acquirers offering DCC results in ever more cardholders being gouged.

Nobody in the payments industry would recommend his mother use DCC when traveling. So why hasn't the payments industry self-regulated and curbed it?

Payment networks and many banks have insulated themselves from DCC fee disintermediation.

## **Ripped off**

Cardholders unaware they've been ripped off rarely complain. Consumers are more comfortable paying in their home currency because it's familiar. Cardholders see the local and their native currency prices and, fleetingly, the exchange rate. They don't however know by paying in the local currency they receive a wholesale exchange rate – 4% or so better than the DCC rate merchants offer.

MasterCard and Visa require merchants offering DCC give consumers a choice and disclose the conversion rate. The European Commission's proposed Payment Services Directive 2 article 52 similarly would require consumers have a choice whether to use DCC and that the exchange-rate be disclosed.

The EC's proposed regulations provide a safe harbour in which DCC will flourish, consumers will continue to be fleeced and the payment networks can rationalize turning a blind eye. Visa EU hides behind the EC's skirt to defend its DCC rules as sufficient.

MasterCard and Visa worry about being charged with suppressing competition in the currency-conversion market. Given Brussels mandarins' hostility to the networks, that's not an unreasonable fear. In 2013 DCC specialist Global Blue filed an anti-competition complaint with the EC Competition Directorate over MasterCard's and Visa EU's DCC rules and compliance fees, contending they're anti-competitive.

Former US Supreme Court Justice Louis Brandeis observed, "Sunlight is said to be the best of disinfectants." The networks curate global payment ecosystems to maximize use. While they could ban DCC or increase penalty fees, they could take their a cue from Justice Brandeis. It would be best to require merchants offering DCC to disclose their foreign-exchange rate and price in cardholders' home currency and the wholesale currency-conversion rate they'd receive paying in the local currency and estimated price in their native currency. No consumer would knowingly pay 4% more simply to have a receipt today in his home currency. The market would swiftly reallocate capital and entrepreneurial talent away from DCC to higher-value activities.

Banks issuing cards have also long profited from rich cross-border-transaction fees. While most card issuers charge foreign-transaction or currency-conversion fees, competition and fee transparency caused some such as Nationwide and Capital One to offer cards with no currency-conversion-markup or foreign-transaction fees. A Capital One cardholder in Paris paying in euros enjoys a wholesale exchange rate. All banks, including those charging cross-border fees, would best serve their cardholders by warning them to avoid DCC.

To protect consumers, the Commission should set aside its abiding dislike of the networks and let them, indeed encourage them to, curb DCC.

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